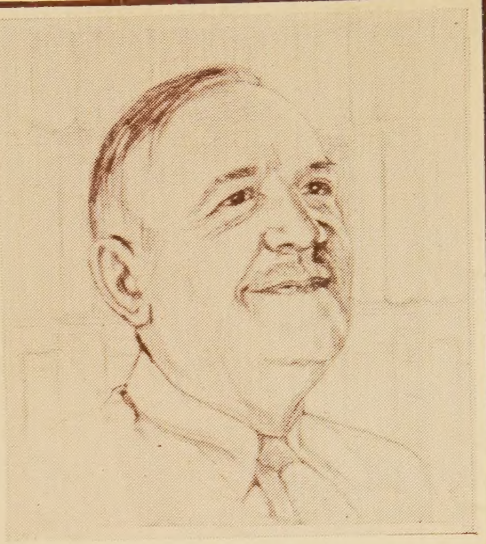
THE DISTRIBUTION AGE

RALPH BORSODI



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THE DISTRIBUTION AGE

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THE DISTRIBUTION AGE

A STUDY OF THE ECONOMY OF MODERN DISTRIBUTION

BY

RALPH BORSODI

AUTHOR OF "NATIONAL ADVERTISING," "THE NEW ACCOUNTING," ETC.

WITH AN INTRODUCTION BY

LEW HAHN

MANAGING DIRECTOR OF THE NATIONAL RETAIL DRY GOODS ASSOCIATION

D. APPLETON AND COMPANY

NEW YORK LONDON

1927

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PRINTED IN THE UNITED STATES OF AMERICA

PREFACE

In the fifty years between 1870 and 1920, the cost of distributing the necessities and luxuries which we consume has nearly trebled, while the cost of producing them has been reduced by more than one-fifth. If the cost of distribution continues to rise at the same rate, before the end of the next fifty years, we shall have more people engaged in the work of distribution—selling, advertising, delivering, transporting, etc.—than we shall have in the work of production, than we shall have occupied in farming, stock raising, lumbering, mining, and manufacturing.

It is evident that what we are saving through the lower costs of modern methods of production, we are losing through the higher costs of modern methods of distribution. The question is, "What can we do about it?"

To answer that question constructively, I have found it necessary, first of all, to make a critical analysis of the distribution elements of the consumer's burden, and to direct attention to certain facts in connection with the marketing and distribution of the products which we consume, the importance of which has not been generally recognized. Most of these facts have to do with what

I call physical distribution and "high power" marketing—the transportation of raw materials and finished products, and the methods of selling, advertising, and financing, which manufacturers today use in an effort to keep their factories "sold up" to maximum capacity of production.

The first and second parts of this book are devoted to this analysis of modern methods of distribution. This study makes it plain that only about one-third of the consumer's dollar spent at retail is paid for production while two-thirds is paid for distribution. What will perhaps be most surprising to those who have made no study of this subject, this study reveals that it is the manufacturers rather than the retailers and jobbers who get the most of what the consumer pays for marketing and that they are principally responsible for the extravagances with which modern distribution abounds.

The third and fourth parts of the book represent an effort to suggest what consumers, retailers, jobbers, and manufacturers can do in order to lower the cost of distribution. These two parts contain suggestions upon which individuals can act immediately—suggestions by which they can make their power as buyers the directing force in regulating the activities of every manufacturer, wholesaler, and retailer. But they also contain suggestions of an even more far-reaching nature —suggestions which should not only result in lower costs of distribution, but which contain the

possibilities for very considerably improving the conditions of living and the cultural level of modern society. Unless the more prosperous consumers of the nation can be persuaded to turn themselves into gourmands, clothes racks, and gasoline-eaters and to devote their lives largely to the consumption of the endless quantities of things which mass production is evoking, we shall have to give a thought to the problem of enabling the poorer sections of society to live as comfortably as industrial progress today makes it possible, as well as to the problem of making it possible for most of us to live richly and beautifully in spite of the imperative need of consuming all that our production machinery is capable of producing.

RALPH BORSODI

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INTRODUCTION

Because I am convinced that our great problems in the field of economics during the next half century are bound to be distribution problems, I am glad that Ralph Borsodi has written this book on "the Distribution Age." It is a book which should be read by all. The retailer, unless he is content to pass out of the picture as an independent factor, must learn what Borsodi is trying to teach, namely that the retailer cannot honestly and effectively serve the consumer by accepting nationally advertised and branded merchandise as the easiest way. The consumer too must interest himself in Borsodi's thesis unless he desires steadily to reduce his own consuming power. And the manufacturer—even the manufacturer most committed to the use of national advertising—owes it to his own permanent success to strain his tolerance to the limit by getting the nub of Borsodi's contention plainly in his mind. The consuming public is a good old steady cow but there is a point beyond which its milk supply must show strong symptoms of failing.

In looking back over the changes that have taken place in the world of business during the last thirty years I am most impressed with the

altered status of the smaller one line retailers. To cite just one line which is typical of others, let me take the retail druggist. A Mr. Andrews was the neighborhood druggist when I was a boy. He was a chemist and because physicians then relied largely on prescriptions he devoted a good portion of his time to that work. In his odd moments he compounded from his own formulae various ointments and lotions and emolients. All these bore his name on labels which now would be regarded as archaic examples of the printer's art, although even now I find myself comparing them, to the advantage of the old druggist, with the torrent of preparations which today is offered to the consumer. The whole neighborhood had faith in the local druggist's preparations and he was a real figure in the community. How his net profit would have compared with that of the modern druggist I do not know. I doubt that any modern drug retailer could have the satisfaction and the respect of his customers that Mr. Andrews enjoyed. He was his own man.

Today that is all changed. Mr. Andrews' preparations have given place to countless rows of proprietary articles all branded and advertised by the big concerns that make them. The work that Andrews and his kind did has passed into the hands of a few large concerns and today every drug store carries exactly the same things. There is no individuality about any drug store that would lead a customer to walk a block out of his

way to patronize one rather than another. Competition among druggists has passed out, except for a certain competition of accessibility and what is left of the competition on price. With the efforts of the manufacturers of these advertised articles to compel all retailers to sell at the same price there isn't much of price competition left either and the druggists thus robbed of their right to be independent agents have joined the clamor of the manufacturers and are shouting to a benevolent national government to eradicate the last and only opportunity for free competition by the enactment of legislation to give the manufacturer complete power to control the retailer's selling price.

Because I sincerely believe that it is not good for the community to have the independent retailer changed into the puppet of the nationally advertising manufacturer I am glad that Mr. Borsodi has made this study of the economic consequences of what he calls "high pressure marketing."

The last half century has witnessed prodigious increases and improvements in the field of production. All the engineering genius of the world has been focused on the job of turning out commodities. Distribution has escaped attention, except that every now and then some one has anathematized the "middleman." During the last decade, especially, there has been a frank avowal of admiration for and faith in the efficacy of a

"Fordized" industry with forced distribution by the producer. Fortunately, this theory is on the way out. It is being replaced with a slightly clearer conception of the fact that the consumer, after all, must have a word or two now and then as to what he wants. The future should redemonstrate the lesson of the past that it is cheaper in the end to produce what the consumer wants and sell it as the normal answer to the demand than it ever can be to make what the manufacturer wants to make and force its consumption by high pressure selling and advertising.

Unless the retailer is the consumer's purchasing agent he has no warrant for existence and if he accepts the position of selling agent for the manufacturer he must pass from the picture. In our economic scheme of things there is an important place for each factor in the chain of production and distribution. It is the manufacturer's job to produce the merchandise. The jobber's task is to carry the stocks. The function of the retailer is to proclaim the merchandise to the consuming public and to sell it with such service as his class of trade requires, at the lowest possible price commensurate with the quality and service which his class of trade demands.

When the manufacturer insists on appropriating to himself part of the function of the retailer by an attempt to control the consumer market he should be very sure that he can prove beyond question that he can fulfill that function

more economically than the retailer can. If he can do that then the retailer must be willing to stand aside, for economic development will thrust him aside whether he is willing or not. The identification of merchandise by branding and the forcing of distribution by national advertising and high pressure selling do not put goods in the consumer's hands at lower prices. Instead they increase the cost and so reduce consumption. Therefore the retailer who hooks himself on to the national advertiser's scheme is betraying his public's trust and selling his own birthright for considerably less than a mess of pottage.

LEW HAHN

PART I

THE COST OF DISTRIBUTION

I

THE DISTRIBUTION AGE

The day is gone when the recipe for fabulous profit was simply "production; more production; still more production!"

The golden age of production is past.

The age of distribution is upon us.

If it is an exaggeration to say that the World War ended the one era—it is no exaggeration to say that it thrust us into the new one.

Under the stimulus of war, American industry discovered that its facilities for production, laboriously improved during the half century since mass and standardized production started during the Civil War, are really capable of producing in endless quantities.

The old machinery, by speeding up, by day-and-night operation, has developed astoundingly greater production capacity. The looms weave cloth more rapidly than we can wear it out. The farmers produce food in greater abundance than we can eat it. The lathes, drills, and punches produce things faster than we can consume them.

New machinery, in unlimited quantities, often to be purchased on a "shoe string"—producing

much more than the old, and more and more automatic—is still further multiplying the capacities of our factories.

The problem which industry today is trying to solve is no longer *how to produce,* but *how to market profitably what it can produce.*

When farmers regularly grow "bumper" crops, and discover that the very fact that they have produced superabundantly results in loss rather than profit for them; when manufacturers have to turn to "high pressure" selling in an effort to keep their factories operating at a large enough percentage of their capacities to meet their fixed costs; when retailers and wholesalers find it necessary to buy from "hand to mouth," and carry smaller stocks to speed turnover to the point which enables them to survive—every part of our economic structure is being strained by the strenuous effort *to market profitably what modern industry can produce.*

To solve this problem, we have literally nothing in the way of clear principles, and less in the way of sound practice. Every factor in distribution is a law unto itself. Every producer fashions methods of distribution to suit himself, quite without regard to their effect upon distribution as a whole.

To the man who looks beyond the immediate moment, who is concerned with the condition which will face society five, ten, and fifteen years from now, it is essential that the principles involved should be clarified.

The need for doing this is imperative.

We have a large and constantly growing body of public opinion, which insists that the cost of distribution is too high, that unnecessary distributors must be eliminated, and that more economical methods must be introduced into distribution.

On the other side, we have the most powerful and influential manufacturers in many lines constantly developing the agencies for selling and perfecting the mediums for advertising on the theory that the solution of the problem requires more and more selling and more and more advertising.

If the retailers and wholesalers of the country continue to be passive factors in the solution of this problem—if they fail to assume the leadership in molding distribution methods and distribution channels, then they will fail to properly serve society, and will earn the inevitable reward of failure—a shrinking return from their business and a lessening influence upon our economic life.

If the manufacturers, who are today the dominant element in the development of marketing and merchandising methods, are permitted to maintain their leadership in distribution, then we shall see a development of brand specification, high pressure selling, and national advertising in the next fifty years by comparison to which existing methods and practices will seem infantile.

We shall see a complete transformation of

manufacturing, and the great assets of our manufacturing establishments will no longer be their production facilities, but their marketing organizations and the goodwill of their brands. Distribution costs will continue to rise. Marketing methods will become more than ever a reflection of the individual necessities of various manufacturers, and even less than today, a reflection of the needs of society. Retailers and wholesalers will become mere slot machines. The public will continue to complain about the profiteering middleman. The high cost of distribution will become the subject of more and more heated debate by congresses and conferences. The ultimate producer and the ultimate consumer may turn in earnest to coöperatives, and coöperation failing, may turn to various forms of governmental distribution.

There is no reason why retailers and wholesalers should reject the opportunity to lead in the solution of this problem. Theirs is the strategic position. They have the necessary organizations —they have even the necessary leaders. What is needed is a greater appreciation and understanding of the underlying economic basis for the rise in the cost of distribution.

It is in the hope that I may be able to contribute something to this aspect of the matter that this book is being written.

II

THE REAL PROBLEM

As I see it, the real problem may be stated as follows:

Why is it that the ratio of distribution costs to production costs is constantly rising? Why is it that in spite of increasing efficiency in transportation, warehousing, banking, credit, accounting, selling, and advertising, the share of the consumer's dollar paid for production is constantly growing smaller and the share paid for distribution larger?

It is not unreasonable for us to expect that the invention of better machines for performing every mechanical step in distribution, and the greater sub-division of the labor of those engaged in distribution, should reduce distribution costs year by year. Progress should lower distribution costs just as progress lowers production costs.

Bigger freight cars and locomotives ought to lower transportation costs, but they do not seem to do so.

Speedy delivery cars and powerful five-ton auto trucks ought to lower drayage costs, but they do not seem to do so.

Larger grain elevators, more efficient cold storage warehouses, better terminal facilities; a better currency and a better banking system; typewriters, adding machines, bookkeeping machines, cash registers—automatic machines for even such trifling operations as stamping and sealing envelopes—all ought to lower the cost of distribution. But they do not seem to do so!

Instead of a lower cost of distribution, we have actually a rising cost of distribution.

Before, however, we try to find out why this is so, we ought to satisfy ourselves first about whether it is actually true that distribution costs have risen out of proportion to production costs. If this problem is to be given serious consideration we ought not to accept as proved what might after all be merely a general delusion. In so important a matter, it is not enough to start with the premise that where there is so much smoke, there must be some fire. It is necessary, first of all, to establish upon very solid ground the facts concerning our premise. We must produce proof as near to demonstration as is possible, that distribution costs really have risen out of proportion to production costs.

But in order to establish the facts—above all, in order to eliminate non-essential facts—it is necessary to define distribution. Pick a group of a dozen intelligent men at random, and no two of them will be likely to have the same conception of distribution. Yet if we are to determine whether

distribution costs have risen disproportionately, and intelligently seek for causes and propose remedies suitable to the real difficulties, it is essential that we define distribution. We must make it possible to distinguish between *the cost of distribution* and *the cost of production.*

Having established the truth as to whether the cost of distribution has risen, and also determined just what constitutes the cost of distribution, we shall then be ready to seek the causes of the rise in its cost.

That we shall find not one cause, but a considerable number of causes, each of which contributes more or less to the total rise in distribution costs is, of course, certain. It will then be necessary to determine the relative importance of the various causes and to select from among them for first consideration those which are most important and which contribute most to the rise in costs.

Then, and only then, shall we be ready to consider possible remedies.

Over a quarter of a century of exceptional experience in business—experience which has given me unusual opportunities for observing and studying nearly every phase of our distribution machinery—makes me say that such a line of study will prove:

1. That distribution costs in this country, both for physical distribution and for marketing, have risen out of proportion to production costs;

2. That high freight rates and cross hauling and

unnecessary transportation are principally responsible for the rise in the cost of physical distribution;

3. That one of the most important factors in causing the rise in the cost of marketing, as distinguished from the rise in the cost of physical distribution, is "high pressure" selling, "high pressure" advertising, "high pressure" marketing generally;

4. That manufacturers engaged in mass production and mass selling have been the active factors in the development of extravagant marketing and unnecessary transportation—that they are responsible for the breaking down of that skillful and skeptical buying by retailers and consumers which tends to raise standards and to lower costs;

5. Finally, that the wastes of "high pressure" marketing could be eliminated and the cost of distribution lowered if the retailers and wholesalers of the country would, first, accept full responsibility for the task of furnishing to the consumers of the nation the products of our farms and factories; second, buy according to established grades and standards in order to make production subservient to consumption; and, third, promote consumer education as to merchandise.

III

THE RISE IN THE COST OF DISTRIBUTION

Is it actually a fact that the cost of distribution has risen out of proportion to the cost of production?

Perhaps the simplest index of the relative costs of production and distribution [1] which we might use would be the numbers of persons engaged in these two occupations.

In 1870, 10% of the population ten years of age and over engaged in gainful occupations—10% of the entire energy of the nation—was engaged in the process of transporting and distributing our commodities. Ten years later, this had increased to 11%. In the next ten years it increased to 14%, and by 1900, it had risen to 16%. This indicates an average rise during the thirty years ending with 1900 of about 1½% per decade.

Beginning with 1900, the rate of increase was progressively more rapid. In the ten years end-

[1] The industries, trades, and occupations as classified in the census were arranged into the two categories of production and distribution merely to furnish an index of the relative growth in these two fields of business activity. The terms production and distribution as used in this chapter do not, therefore, exactly correspond with the special definition of those terms used later in this book.

ing with 1910, it jumped to 20%, an increase of 4%, and in the ten years ending with the census of 1920, it jumped to 25%, an increase of 5% for the decade, or ½% per year.

During the same fifty years, the portion of the population engaged in production decreased from 69% to 60%. In the twenty years from 1900 to 1920 it remained practically stationary. In other words, since 1900, when the energy devoted to distribution began to increase most rapidly, the energy devoted to production has stood still.

TABLE 1

Population 10 Years of Age and Over Engaged in Gainful Occupation

Census	Production	Per Cent	Distribution	Per Cent	Professional, Public and Domestic Service	Per Cent	Total
1870	8,629,892	69	1,191,238	10	2,684,793	21	12,505,923
1880	11,498,601	66	1,871,503	11	4,021,995	23	17,392,099
1890	14,826,916	64	3,326,122	14	5,165,145	22	23,318,183
1900	17,467,074	60	4,766,964	16	6,839,195	24	29,073,233
1910	23,375,446	61	7,605,730	20	7,186,160	19	38,167,336
1920	24,861,905	60	10,433,102	25	6,319,241	15	41,614,248

Table I gives the figures not only in percentages, but also in total number of persons. It shows that, while the 8,629,892 persons engaged fifty years ago in production practically tripled their number by 1920, the 1,191,238 persons engaged in trade and transportation increased to nearly ten times the original number.

By eliminating those engaged in professional, public, and domestic service, as is done in Table II, and comparing only the numbers engaged in

TABLE 2

Population 10 Years of Age and Over Engaged in Production and Distribution

Census	Production	Per Cent	Distribution	Per Cent	Total
1870	8,629,892	88	1,191,238	12	9,821,130
1880	11,498,601	86	1,871,503	14	13,370,104
1890	14,826,916	82	3,326,122	18	18,153,038
1900	17,467,074	79	4,766,964	21	22,234,038
1910	23,375,446	75	7,605,730	25	30,981,176
1920	24,861,905	70	10,433,102	30	35,295,007

production to those engaged in distribution, this index shows a drop in human energy devoted to production of from 88% to 70% during a period when energy devoted to distribution increased from 12% to 30%.

This index, however, ignores the fact that the relative wages and salaries paid to those in the two groups are not the same today as was the case fifty years ago. Fifty years ago, salesmen and clerks, railway men and drivers, and all others engaged in distribution, were not so well compensated as they are today. Today, salesmen and advertising men are much better paid than craftsmen and superintendents, and they enjoy an increasing premium as business attaches more and more importance to distribution and less and less to production. It should therefore be borne in mind that not only have the numbers engaged in distribution increased, but their average compensation has increased more rapidly than the average compensation of those engaged in production.

Plates I and II show graphically the gradual

decrease in the ratio of energy used in production and the corresponding increase in the ratio of energy used in distribution.

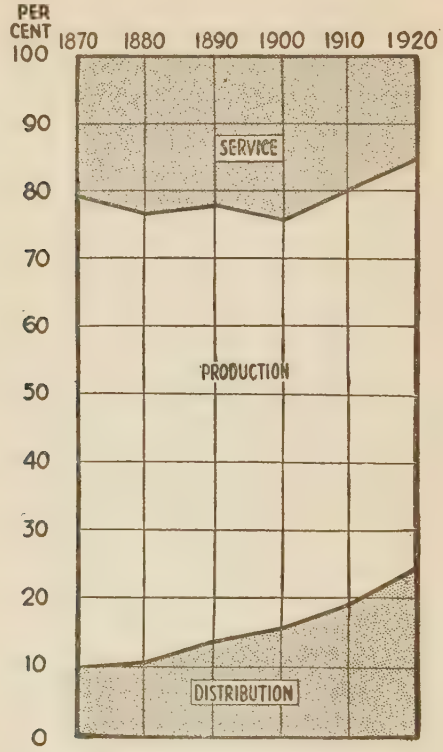


PLATE I

Index of Relative Cost of (a) Professional and Domestic Service, (b) Production, and (c) Distribution, 1870 to 1920

Even at this rate of progression, we shall within the next fifty years have one man engaged in distribution and transportation for every man

who is engaged in farming or manufacturing. As a matter of fact, it is exceedingly probable that we shall attain this situation within the next

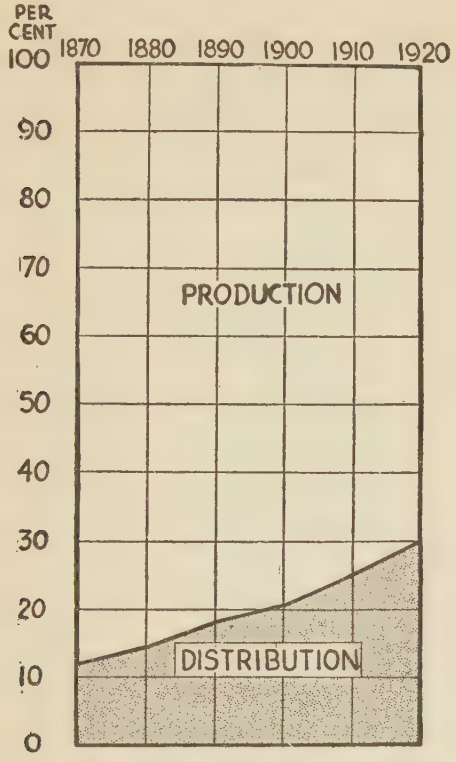


PLATE II

Index of Relative Cost of Production and Distribution, 1870 to 1920

twenty-five or thirty years, because the increase in the population devoted to distribution is progressively greater each year.

Since human energy is always paid for, it is perfectly obvious that when we buy anything today we are paying proportionately much more for distribution and much less for production than we were fifty years ago.

In addition to the economic loss involved in this change, an even more melancholy fact is disclosed by the figures in Table I. The numbers engaged in distribution are evidently being recruited almost entirely from the ranks of those who normally should engage in professional, public and domestic service.

Our university graduates are in increasing numbers turning to business life rather than to professional life. Socially, a successful advertising man rates higher than a successful professor. Impressionable youth makes the former the object of hero-worship rather than the latter, and naturally money making becomes its goal in life rather than social service.

Only one field of endeavor in the United States is in more need of new and idealistic blood than teaching and preaching and the professions generally. That is, of course, the field of cookery and domestic economy. And this field is also being drained of promising cooks and housekeepers in order that the demand for sales-clerks and stenographers may be supplied.

Present tendencies force potential artists, scientists, doctors, architects, teachers, and writers to become salesmen and advertising men. They

drive cooks and domestics out of homes and make them wait on us behind counters. Isn't this a process which involves a real sacrifice of culture and comfort?

IV

WHAT IS DISTRIBUTION?

One of the strange things in connection with the National Distribution Conference held under the auspices of the United States Chamber of Commerce, in 1925, was that while the word "distribution" was on everybody's lips, nobody in attendance at the conference thought it necessary to agree with anybody else as to what they meant by the word. To a great many of the conferees, it meant only wholesaling and retailing; but to some of them it meant transportation; to others, it meant selling and advertising. If a general connotation might be distilled from the meanings ascribed to it by this group of about two hundred and fifty men called together expressly to discuss distribution, it would have to be in a vague fashion, the handling of merchandise after it is a finished commodity.

So vague a definition, if it may be called a definition at all, is of course worthless. If we are to seek the causes of the high cost of distribution, we must first of all determine what is, and what is not, properly a part of the cost of distribution. Production costs must be sharply differentiated

from distribution costs, and from any other kinds of costs which would tend to confuse our thinking upon the subject.

We shall then see, first, that not only manufacturers, but also retailers and wholesalers are engaged in production; and secondly, that not only retailers and wholesalers, but also manufacturers and producers are engaged in distribution. We shall have to seek therefore for the causes of the rise in distribution costs not only by studying the merchandising methods of retailers and wholesalers, but also by studying the marketing methods of manufacturers.

There are two uses of the word distribution which must be clearly differentiated at this time; first, the use of the word to describe physical distribution such as transportation and storage; second, the use of the word distribution to describe what is better termed marketing.

There is a third use of the term—the special and technical sense in which it is used in pure economic science—which might be called income distribution. In this sense distribution is the process by which the total income of the entire nation is apportioned to labor and capital and to all the factors which contribute to its production. It therefore has to do with rent, wages, interest, and profit; their nature; their relationship one to another; and the economic validity of the proportion which is paid out to labor, to land, to capital, and to management. Income distribution treats

the subject of physical distribution and the buying and selling of goods, the questions in which we are at present most interested, from a standpoint with which we are not here concerned.

PHYSICAL DISTRIBUTION

What I shall call physical distribution is that part of the complete process of distribution which is involved in the transporting and storing of goods. The cost of physical distribution is the cost of transporting goods from the places of production to the places where they are to be consumed, of storing them in warehouses and stores until such time as consumers are in need of them, and the overhead expense incidental to these two processes. This cost is a part of the total cost of distribution which has to be distinguished from the cost of marketing in order to make clear the relative responsibility of transportation and marketing for the rise in the cost of distribution. To determine whether a very large part of the rise is caused by "high pressure" selling, advertising, and marketing by manufacturers who desired to operate to a capacity in excess of the current demands of the market, it is necessary to separate the cost of physical distribution from the cost of marketing.

MARKETING

Buying and selling are necessary adjuncts to our present system of distribution. The cost of

buying and selling and the overhead incidental to it, principally advertising, traveling, clerical and office expenses, I shall call the cost of marketing.

Methods of buying and selling today are the result of a gradual evolution from earlier methods when production, distribution, and consumption were almost entirely local, and when each community was practically self-sustained. When the farmer took his wheat to the local grist mill to have it ground, and took away the meal himself, no complex marketing system was necessary. Today the farmer has to sell his wheat to a local elevator, and the cost of this step in distribution is the first in a long series of distribution costs which represent in the aggregate a sum far in excess of that which prevailed years ago. In fact, many of our present day marketing costs are for operations which could hardly be said to have any existence at that time.

The introduction of modern machinery and of modern labor-saving methods after the Civil War did not immediately result in any great increase in the cost of marketing, nor did it require men to devote more time to the performance of this work. At first the demand for manufactured goods was in excess of the production and the manufacturer had only three problems—to make, to deliver, and to collect.

"For a considerable time," says the Report of the Joint Commission on Agricultural Inquiry on

Marketing and Distribution, "the demand exceeded the capacity of manufacturers, and the entire effort was to devise improved methods of mechanical production." [1]

When, however, production began to exceed the capacity of the markets to absorb the commodities being made and manufacturers found it necessary to create additional markets for their products, marketing became one of the serious problems of manufacturers.

Today it is a problem which exceeds in importance that of production. The greater part of the average manufacturer's thought is engrossed with this problem, and a considerable portion of the manufacturer's total expenditures is today devoted to marketing his production. A large part of the capital of many manufacturers is represented by investments made to maintain a market for their production. In addition to securing a price sufficient to cover direct expenditures for selling and advertising, manufacturers must earn profits to pay dividends upon this part of their investment of capital. What manufacturers receive for their product today is therefore a payment proportionately less for production and proportionately more for distribution. Manufacturers are distributors, not merely producers.

If a farmer spends half his time in growing

[1] Report No. 408, House of Representatives, 67th Congress, 1st Session.

vegetables, and half his time in huckstering, then in spite of the fact that he is called a "producer," only half of his time may be properly chargeable to production. Half is just as truly distribution as if the selling of vegetables had been performed by a green goods grocer.

If a manufacturer maintains an extensive staff of traveling salesmen, conducts an expensive national advertising campaign, and finally, earns immense profits because of the demand for his trade-marked brand, the portions of his gross margin which he devotes to marketing and the profits earned by reason of his marketing skill, are distribution costs even though he is, like the farmer, generally called a "producer."

For the same reason that it is important to distinguish between the manufacturers' cost of production and their cost of marketing, it is important to distinguish between what we may call the productive margin of wholesalers and retailers, (what they are in reality paid for the physical distribution of the merchandise they handle), and their margin for merchandising, (what they are paid for selling, displaying, advertising, and similar costs of merchandising.)

The public's general impression that the entire sum paid to wholesalers and retailers is non-productive, while the sum paid to manufacturers for goods is productive, makes it necessary to distinguish carefully these two groups of costs.

The cost of transportation is obviously not a

marketing or merchandising cost. Neither is the cost of warehousing, without regard to whether the expense for storage is incurred by manufacturer, wholesaler, or retailer. Physical distribution is a process of producing time and place utilities, just as truly as mining, farming, or manufacturing are processes of producing basic and form utilities. The work of adding these time and place utilities to finished products is an integral part of the productive process. It is production when it is done by manufacturers. And it is production when it is done by retailers and wholesalers.

To establish the fact that these are really parts of the productive process, it is only necessary for us to give a little consideration to the four recognized stages of production and the utilities or values created at each stage.

BASIC UTILITIES

The raw materials of commerce are the basic utilities of economics. Wheat, corn, and oats; cotton and wool; coal and iron—these are basic utilities, and farming, stockraising, mining, fishing, in fact every operation which results in the production of our basic commodities is a part of the process of producing basic utilities.

FORM UTILITIES

Raw materials, however, are rarely ready for consumption as they come from the basic pro-

ducer. With the exception of products such as fresh vegetables, fruits, nuts, eggs, and milk, every basic utility is fabricated before it is ready for consumption. This applies to vegetable and animal products such as cotton, flax, wool, and hides, which have to be made into cloth, clothing, and shoes, and to mineral products such as iron, copper, zinc, lead, and oil, which rarely reach the ultimate consumer in the form of raw material. While some of the processes of fabricating or changing the form of raw materials are performed by basic producers, the overwhelming majority of products are processed and fabricated by millers and manufacturers.

PLACE UTILITIES

The production of basic utilities and their fabrication into finished products usually takes place where it can be done most economically and therefore most profitably. Cotton is not grown in the north because there it would be necessary to produce it in green houses. For the same reason—economy in production—steel is produced in great quantities in Pittsburgh and little or none is produced in New York. It can, of course, be produced in New York City, but only at greatly increased cost. Value or utility is therefore added to the Pittsburgh steel by transporting it from the point of fabrication to the point of consumption in New York which is equal to the dif-

ference in the cost of producing in New York and the cost of producing it in Pittsburgh.

All transportation of goods, regardless of whether the goods are in the raw state, semi-finished, or finished, since it results in the placing of the goods where they can be used or consumed more economically than at the point of production, involves the creation of place utilities.

Cotton on the farm is a mere basic utility. Transported in the farmer's wagon and then by freight to the cotton mill, the process of moving it from the farm to the mill has added to its utility. In the same way when woven into a finished cloth, its transportation from the mill to the store where it is convenient for a consumer to buy it, adds to its value. The cost of transporting goods from one place to other places where they are more valuable is the cost of creating place utilities. This cost and the cost of producing time utilities together make up the cost of what I have called physical distribution.

TIME UTILITIES

There is nearly always a "lag" between production and consumption which makes storage of goods essential. Consumption of most products is generally a continuous process, while production is often an intermittent one. Goods therefore have to be stored until the consumers are ready to use them. The value which is thus added

by storing commodities is a value resulting from the creation of time utilities.

The cost of maintaining and operating the elevators in which our cereals are kept, the huge oil tanks in which gasoline and kerosene are stored, the warehouses in which manufacturers store raw materials, and in which they accumulate their finished products, the cost of the warehouses in which jobbers and wholesalers keep supplies of all kinds of commodities, and finally, the cost of the store rooms and the space in retail stores devoted to shelves and counters and display cases containing goods, are all costs incurred for the creation of time utilities.

The storage warehouse industry brings up to most people merely a picture of cold storage. Our cold storage warehouse system is a gigantic industry, it is true. Yet the value of the time utilities created by the cold storage and public warehouse industry is relatively trifling in amount compared to the values created by farmers, manufacturers, wholesalers, and retailers in storing goods until the time comes when consumers can use them.

In the case of the retailers, the major proportion of what they spend for the rent of their stores is, of course, actually devoted to the selling and displaying of their merchandise. But every retail store has storage rooms which are not used for selling and the rent paid for such space and for the space used for storing goods on shelves,

under counters and in display cases represents expenditures for the creation of time utilities. To determine exactly the cost of creating time utilities, rents have to be divided into two parts, one part—the cost of creating the time utilities—being for the space actually occupied by goods, and the other—the cost chargeable to marketing or merchandising—being for the space used exclusively for selling.

A similar division into two parts would naturally have to be made of the time of those working in every stage of production and distribution in accordance with the time devoted by them to the care of goods, and the time devoted to actual selling. Labor devoted to the storage and care of stock is labor devoted to the creation of time utilities. Labor devoted to actual selling is labor devoted to marketing or merchandising. Because there is no practical necessity for making this division in day to day bookkeeping, we have failed to recognize the importance of the distinction. But to get to the truth about distribution, it is necessary to keep from confusing the two costs. One is the cost of producing a time utility—the other is a marketing or merchandising cost and not a physical distribution cost.

The creation of any of the four utilities is an operation which produces values. Their creation is production. There is absolutely no excuse, therefore, for considering the production of time

and place utilities as any less production than the creation of basic and form utilities.

The fact that the greater part of the time and place utilities which are consumed are created by our so-called middlemen, the retailers and wholesalers, has tended to blind us to the fact that in this part of their work, retailers and wholesalers are engaged in production.

All of what we pay to retailers and all of what we pay to wholesalers should not, therefore, be considered payment for distribution, any more, as we shall see, than all of what we pay to manufacturers should be considered payment for production.

To distinguish the work of creating time and place utilities from that adjunct to the process of distribution which I have called marketing, I have called the process of creating these two utilities the work of physical distribution. It is true that, from the standpoint of pure economics, marketing, since it is necessary to the regulation of production and the distribution of the goods produced, can ultimately be resolved into the four utilities and in that way considered a part of the process of production. From the standpoint of our immediate inquiry, however, we shall see that the distinction is very important.

This distinction becomes clear if we divide the expenditures of wholesalers and retailers into three groups: (1)Such items as interest on investment in stock, depreciation on stock, stor-

age of stock, freight, and delivery, which are almost in their entirety incurred for physical distribution, are expenses incidental to the pure and simple creation of time and place utilities. (2) Items of expense such as rent, bookkeeping, and credit, are partly chargeable to physical distribution and partly to merchandising. (3) Items such as advertising, window display, salaries of salesmen and buyers, and all items of expense which are directly involved in the buying and selling of merchandise, are entirely merchandising or marketing costs.

A careful analysis of retailers' costs indicates that if divided in this way about one-half of the total is chargeable to merchandising. About half of what we pay to the retailers of the country, therefore, is spent for what every economist must acknowledge to be production, and only half for what the general public believes to be non-productive.

On the other hand, the prevalent notion that what is paid to the manufacturers of the country represents payment for production only is a fallacy. In many cases, as we shall see, a large part of the sum the manufacturer is paid for his product is used to cover distribution costs.

The habit of using distribution as a synonym for retailing and wholesaling is responsible for much confusion about the responsibility for the high cost of distribution. The belief that distribution begins only after goods have been fabri-

cated and are ready for use by the ultimate consumer is responsible for the belief that while retailers are distributors, manufacturers are producers. The truth, of course, is that both are both producers and distributors.

Every factor in the process of production is engaged in distribution just as truly as is the retailer and wholesaler.

The farmer who grows cotton, (surely no one will question his status as a producer) must move it from his fields—where there is no way for using it and it is practically valueless—to the cotton gin and then to his local warehouse or shipping point so that he may market it. The grower is thus not merely a producer of a basic utility—cotton—but a creator of time and place utilities —and these operations all involve distribution.

The factor, broker, and cotton merchant, who in turn buy and sell, and assemble the cotton, are all engaged in distributing it.

The cotton mill which fabricates the fiber into cloth, (surely no one will doubt that the mill is a producer), is also engaged in distribution. The mill not only transfers cotton, from the warehouses in which it is assembled, to the points where it can be spun and woven economically, but it stores the raw cotton until such time as it is ready to weave it, and then repeats both the storing and shipping after it has woven it into cloth. In other words, the cotton mill in buying its raw material and selling its finished product

is involved first in the distribution of the raw cotton, and then in that of the woven cotton cloth.

Distribution, then, is not a process which begins after the cotton has been woven and finished—after its conversion into a form ready for use by ultimate consumers. It does not begin after it is in the hands of wholesalers and retailers. It is a process inseparable from production. It begins when raw materials are marketed and assembled for fabrication. It continues when the finished products are marketed and distributed by manufacturers. It ends when the retailer merchandises goods and delivers them to the ultimate consumers.

Whoever sells and whoever buys is engaged in distribution. Whether he grows cotton, spins cotton, weaves cotton, converts cotton, wholesales cotton, or retails cotton—he distributes cotton.

It is the sum of all the transportation, storage and marketing costs involved in moving goods from the producers of the raw material to the ultimate consumer and making them available when and where they are needed or desired that gives us truly the entire cost of distributing any product.

And since the producers and manufacturers of the nation market and distribute goods, it follows that they have marketing and distribution costs, and that we must compare their costs with the costs of the wholesalers and retailers in deter-

mining whether the distributors or the manufacturers are making distribution cost so much.

Nine-tenths of all the problems of the world would solve themselves if time were taken to properly state them and to define the terms in which they are stated.

No better illustration of the truth of this can possibly be found than in the discussion of this question of the rise in the cost of distribution.

If the rather detailed definitions upon which I have been dwelling have been tedious, I think I can justify the tedium because they should have established the soundness of the following propositions:

(1) That what is usually called distribution refers to two entirely distinct things, one of which I have called physical distribution, and the other marketing;

(2) That physical distribution is an integral part of our productive processes and that if this kind of work is production when it is performed by a manufacturer, it is also production when it is performed by a retailer or wholesaler:

(3) That both manufacturers and retailers, or if you prefer the terms, our producers and distributors, are engaged both in the physical distribution and in the marketing of the products of the country;

(4) That it is necessary to separate the cost of physical distribution from the cost of marketing in order to determine the relative responsibility

of our transportation systems on one hand and of manufacturers and distributors on the other for the rise in the cost of distribution;

(5) That the cost of marketing by manufacturers must be compared to the analogous costs of wholesalers and retailers in order to determine the relative responsibility of the manufacturers and the distributors for the rise in the cost of distribution.

V

THE CAUSES OF THE RISE IN DISTRIBUTION COSTS

Perhaps a brief summary of the argument which forms the basis of this analysis of distribution may be worth while before we turn from the question of "what" distribution is to the question of "why" it costs so much.

The distribution process, that infinitely complicated process by which finished goods move step by step from the producer of the raw materials through brokers, fabricators, wholesalers, and retailers to the ultimate consumer—is really a series of marketing and merchandising and transporting and storing operations.

Distribution begins with the producer.

The producer of a raw material such as cotton, under our present economic system, must sell his cotton. He must devote time to the selling and storing and delivery in order to market his cotton, and the costs which he incurs in marketing, storage, and delivery are the first costs in the distribution of cotton. Every factor, in the same way, who handles the raw cotton, including the weaver and converter of the cotton

fabric, has to market, ship, and store the cotton and the costs which he incurs in these marketing operations are all costs for performing various steps in its distribution. Finally, the costs of merchandising or marketing by wholesalers and retailers determine the cost of performing the last step in the work of distribution. A true and complete total cost of distribution is therefore the total cost of marketing by all the factors involved in distribution from the producer of the raw material to the consumer of the finished product.

It is a common error to assume that the cost of distribution consists only of the cost of doing business by retailers and wholesalers. As a matter of fact, for a real understanding of the causes for the rise in the cost of distribution it is necessary to recognize the greater importance of marketing early in the process of distribution, because if there are excessive costs in the early stages of the process, they are pyramided continuously at every advancing stage, until finally, what may have been only a small excess cost in the beginning has become in the end a large part of the entire cost of the product.

Of the total energy of the nation, less is now devoted to the production of goods than was the case fifty years ago, but much more to their marketing.

Each farmer today, thanks to the modern tillage and harvesting machinery, to tractors and

automobiles, produces more than a dozen farmers produced fifty years ago. In spite of the fact that the population which we feed increases year by year, the number of farmers needed to produce what we eat decreases year by year.

The cost of producing our basic utilities has not, therefore, increased relative to all other costs.

But neither has the cost of producing form utilities, or place utilities, or time utilities.

Modern factories employ less labor per unit of production; modern railways employ fewer workers per ton mile of freight transported than was the case when mass production was in its infancy and goods, if shipped at all, were transported in Conestoga wagons.

If human energy is used as an index of costs, then costs of production are less today.

More people are engaged in distributing raw materials than were engaged fifty years ago—fewer in producing them. More people are engaged in distributing the finished products produced by our factories—fewer in producing them. And more people of course, are engaged in retailing and wholesaling than fifty years ago.

If human energy is used again as an index of costs, then the cost of distribution is higher today.

Production costs less today than fifty years ago —distribution costs more.

Let us now see why this change has taken place,

and why this change continues at a constantly increasing rate.

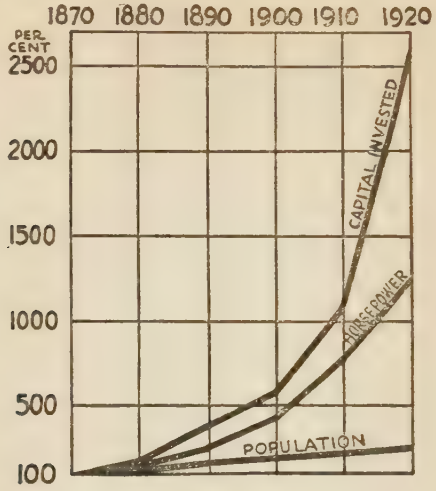


PLATE III

Relative Increase in Manufacturing Facilities and Population, 1870-1920

In 1870, the primary power used exclusively in manufacturing was 2,346,142 horsepower. By 1920, it had risen to 29,504,792 horsepower. In fifty years it increased more than one thousand per cent, in total horsepower. At the same time the quantity of goods which could be produced for each horsepower used in driving machinery was increased almost beyond measure.

The capital invested in manufactures in 1870 was $1,694,567,015. By 1920 this had increased to $44,466,593,771. No allowance has been made in these figures for the decrease in the purchasing

power of the dollar. For one reason, because the dollar invested in 1920 bought proportionately more productive machinery and erected proportionately more efficient factories.

The purchasing power of 1870 dollars may have been twice as great as the purchasing power of 1920 dollars, but the factories erected with 1920 dollars are capable of producing much more than twice as much as factories which the 1870 dollars erected.

During this same fifty years, the population increased only from 38,588,371 to 105,710,620.

Using the year 1870 as a base, the population has grown 174 per cent., horsepower has grown 1158 per cent., and capital invested has grown 2524 per cent. This is shown graphically by census years in Table III.

TABLE III

Relative Increase in Manufacturing Facilities and Population, 1870–1920

Census	Capital Invested in Manufactures	Per Cent	Primary Horsepower in Manufactures	Per Cent	Population	Per Cent
1870	$ 1,694,567,015	100	2,346,142	100	38,558,371	100
1880	2,790,272,606	165	3,410,837	145	50,155,783	130
1890	6,525,050,759	385	5,938,635	253	62,947,714	163
1900	9,813,834,390	579	10,097,893	430	75,994,575	197
1910	18,428,269,706	1,087	18,675,376	796	91,972,266	239
1920	44,466,593,771	2,624	29,504,792	1,258	105,710,620	274

In other words, each consumer today has to consume the products of .2791 horsepower, as compared with .0608 in 1870, or four and one-half times as much as the consumer of fifty years ago. Actually, he has to consume much more than four and one-half times as much, because of the enor-

mously greater output of each horsepower used in production today.

But he must not only buy more than four and one-half times as much in goods. He must pay proportionately a higher price for interest and dividends on the capital being used by the manufacturers. Horsepower increased four and one-half times, but capital invested increased in the same period over twenty-six times. The prices paid by consumers today must therefore include interest and dividends upon over twenty-six times the capital used by manufacturers fifty years ago.

There is no good reason for believing that the next fifty years will see any great change in the growing disproportion between increasing facilities for manufacture and increase in population. On the contrary, a lower birth rate and the restriction of immigration are reducing the rate of increase in population. If manufacturing facilities increase in the future at the same rate as during the past fifty years, the disproportion should become greater and greater year by year.

Assuming that the rate of increase will be the same in the next fifty years as in the ten years between 1910 and 1920, we should have by the year 1970 the amazing situation of a population increase of only 799 per cent., of a horsepower increase of 8,038 per cent., and of a capital invested increase of the fantastic amount of 25,779 per cent.

This speculation as to what may happen in the

next half century may be discounted as much as any one desires, and yet one will be driven to the conclusion that the strenuous present day competition for markets is mere child's play compared to the struggle in which the next generation will be engaged.

A full grasp of the significance of the nation's growth in capacity for production explains the intense competition for markets among manufacturers today. All this production machinery must be kept producing at least to such a percentage of its possible capacity as will yield an adequate return upon the investment in it. The only reason it is not all operated to full capacity is because the quantities of goods which would then be thrown upon the market would result in price declines to catastrophic levels.

Unfortunately, instead of lessening the intensity of the competition, operation of all this machinery at part of capacity actually intensifies it. The effort to sell is naturally intensified in proportion to the idleness of factories.

The manufacturer producing to 90 per cent. of his plant capacity is spurred on to sell the additional 10 per cent. capacity of his plant only by the desire for additional profits. Selling 90 per cent. of his capacity will yield him a satisfactory profit. Selling an additional 10 per cent. simply increases the amount of his profits.

But a manufacturer who is selling to only 50 per cent. of his plant capacity may be driven to

secure even so little as an additional 5 per cent. of business by the dire necessity of getting it or of going bankrupt. Selling only half the capacity of his plant means that he is losing money. If 5 per cent. more business will enable him to break even, he will get that 5 per cent. even though he has to cut the heart out of his normal margins in order to get it.

It is difficult to estimate how large a part of the nation's production facilities are normally in use. One particularly able observer of economic tendencies, Colonel Leonard P. Ayres, uses the number of blast furnaces in operation as a barometer of business conditions. When blast furnaces are in 60 per cent. operation, conditions are normal. When this figure is exceeded, productive industry is experiencing a period of good times; and when it falls below that figure, it is in for a period of hard times.

It is obvious, if 60 per cent. represents normality, that consumers of such a basic commodity as pig iron must pay dividends upon an investment capable of producing two-thirds more pig iron than the country uses in normal times. It needs no great exercise of the imagination to appreciate how pressing the urge to sell must be, how intense the competition when manufacturers are confronted with the problem of earning dividends under such conditions.

The estimated capacity of the country's flour mills as a whole is approximately two and one-

half times the largest production, according to Edmund Brown, Jr.,[1] who made a study of the grain trade for the Federal Trade Commission. Apparently there are ten milling companies which could under pressure produce half the flour made in the United States in an ordinary year.

Our steel plants are now equipped to produce 70 per cent. more steel than the normal requirements of the market.

Our shoe factories have an excess capacity of 80 per cent.

Our copper smelters an excess capacity of over 100 per cent.

While our lumber mills have an excess capacity of over 300 per cent.

Even the automobile industry,—one of our youngest big industries—has a capacity 80 per cent. greater than the ability of the market to absorb automobiles.

While in the textile industry,—one of the oldest industries—we find rayon manufacturers increasing the capacity to produce fabrics from this new fiber by leaps and bounds,—at the very time when cotton mills, woolen mills, and silk mills, have each of them enormously greater capacities for producing fabrics than it is possible for the market to absorb.

But over-capacity for production is not confined to machinery operation in what is each industry's normal working day. Many industries

[1] "Marketing," p. 52.

are organized to operate night shifts which very nearly double the existing over-capacity for production with the same equipment, the same machinery, and the same buildings, while those which are organized on a twenty-four hour basis can very nearly triple a volume of business which is already in excess of the ability of the market to absorb their products.

Is it any wonder that the manufacturers today are more concerned about the problem of marketing than about the problem of producing? No matter how amply supplied the markets may be, they must be made to absorb more and more of the products of our factories. No matter how much the consumer who can afford to buy may resist, he must be made to eat more, to wear out more clothes, to take more drugs, to blow out more tires. He must consume, consume, consume, so that our industries may produce, produce, produce.

As a writer in a business paper [2] puts it, consumers are the

"—central target for a veritable barrage of psychic fire. From all sides, it seems, our emotions are being peppered, our intellects sprayed, our desires shot up by a stream of quick-fire appeals that in our lucid moments appear ominous if not disastrous to any sort of meaningful, reasoned existence. In our ears is the roar of brands, before our eyes a mad dance of trade-marks. Assured by this bill-board that Jimson makes pluperfect

[2] J. G. Berrien in *Sales Management*, April 4, 1925.

pickles, we are lapelled by that newspaper to the effect that no pickles in the universe are the equal of Timson's. Here is the ultimate in motor-car manufacture, says this magazine, only to come to another ultimate a few pages further on. It is all very confusing and getting more so every day."

How are our industries meeting their imperious need of making more sales, of extending their market, or distributing a large enough part of what they produce to operate profitably?

The good old times, when factories were unable to produce goods fast enough for a population used to handicraft production, are gone.

It took over a century to invent the necessary machines, develop efficient methods of spinning and weaving, and secure the capital for the production and erection of our cotton mills.

It took the cotton industry all that time to multiply its machinery for production to the point where spinning and weaving and finishing facilities were in excess of the needs of the market.

During most of that century, the cotton manufacturers had a comparatively simple marketing problem. Their real problem was not marketing, but production—production at low enough costs, production in sufficient quantity.

Contrast the time it took this old industry to develop a surplus of manufacturing facilities with a new industry,—the radio industry—which has had its gestation, birth, growth, and maturity in

recent years. In less than a year after tubes, receivers, and loud speakers were standardized and put in mass production, capital had flowed into the industry in such quantities,—facilities for production grew to such magnitude—that the surplus production of manufacturer after manufacturer had to be thrown upon a demoralized market.

Not only does our technical advance make it easier today to overproduce, but the greater mobility of capital and the vastly greater quantity of capital seeking investment make doubly certain that facilities for production will always be in excess of actual demand for goods. Old industries and new industries are both thus confronted by the imperious need of selling more goods. The potential supply of products is always greater than the immediate demand of the market.

Sales in profitable volume must be secured. If consumer resistance exists—it must be broken down with national advertising. If existing channels of distribution can not be made to take additional volume, new channels must be blasted in which to move the manufacturer's products. If existing markets refuse to absorb all of the production, new markets must be created. If the natural market of a manufacturer—the local territory which is near his factory and which it is most economical for him to supply—does not yield sufficient sales, then the entire nation must

be invaded. An intense competitive warfare is then waged, not only with manufacturers situated in the "foreign" territories, but with all the manufacturers who are after the national market. And, if the national market does not yield sufficient sales in the way of business, then the international market must be invaded.

Foreign trade, like domestic trade, when it consists of an exchange of the products which one country can produce more economically than another, is of course a gain to both. From the standpoint of good international relations, however, it is not a desirable thing that nations should be industrialized to such an extent that the quest for foreign markets precipitates those international rivalries in which wars readily breed.

Yet we might as well face the fact that we are already industrialized to just that extent.

Up to the beginning of the period which we have to face now, our population—thanks to immigration—increased with amazing rapidity. The demand of the domestic market was therefore sufficient to absorb a large enough part of our total production to enable our factories to operate profitably. In addition, our wealth in natural resources enabled us to pay the masses (who constitute the bulk of our consumers), such exceptional wages for labor that they have been able to increase their consumption year by year and thus utilize some of our increasing capacity for production.

Our population, however, in the next fifty years will not increase so rapidly. Nor will our superabundant natural resources last forever—though we shall not probably feel the effects of their disappearance very soon.

With a comparatively static population, we shall sooner or later be driven to enormous increases in exports if our factories are to be kept busy. Yet our whole economic organization is at present devised to prevent exports. Our tariff, our merchant marine, are all mercantilist in their conception and development.

But assume that we abolish the protective tariff, build a merchant marine, organize adequate foreign credit facilities, and turn to exports as a means of keeping our factories busy. Isn't the relief which we may secure certain to prove a rather brief respite?

We may extend the period of this temporary relief by accepting securities in payment for our exports and in effect exporting capital. But we cannot export goods indefinitely without importing goods in payment. If we refuse to accept goods in payment, as in effect we are doing at present with a protective tariff, and ask our foreign customers to give us securities in payment —sooner or later the payments of the interest on the securities will have grown to such volume that the acceptance of the interest would find us importing goods in greater quantity than we would

be exporting goods. There is no escape from this dilemma.

We might try to maintain the exports of our factories by a policy of undermining the industrial production of the nations to whom we export; of keeping them in economic vassalage. We might try "dumping" as a means of preventing the development of competing industries in those nations. Dumping, however, is a sort of international dynamite. When more than one nation begins to play with it, its repercussions interfere with dividends from the foreign markets.

What I have inelegantly referred to above as "dumping," is the exporting of surplus production in order to break into foreign markets which are already adequately supplied by their own industrial organization. In dumping, the foreign factories cut prices below the point at which the local factories can maintain themselves. After the local factories have been destroyed or absorbed, the foreign factories have the local market to themselves.

Dumping, however, is not confined to international trade. Domestic dumping is far more prevalent. It does not always take the form of price cutting, however. Generally, the domestic "dumper" operates with elaborate branch offices, high pressure salesmen, and national advertising. He raises prices, instead of cutting them, and justifies the higher prices by giving "service" of some kind.

International dumping, if it arouses national or racial antagonism, results in war. Domestic dumping results, less dramatically, in higher distribution costs.

If domestic dumping resulted merely in raising the marketing costs of the factories which turn to high pressure marketing as a means of securing sufficient volume to operate profitably, it would not result in a general rise in the cost of distribution. It is the effect of this high pressure marketing upon our whole distributing machinery which is important.

Whenever a factory turns to high pressure marketing, the regular channels in which the products it makes are distributed are subjected to assault and battery. Existing channels are duplicated. Entirely new kinds of channels, many of them more costly than the old, are brought into existence. The old channels then cease to operate in their accustomed manner. The total volume of business is divided between new and old channels. Costs of distribution are raised not merely on the new product, but also on all old products which are handled.

The creation of each new channel of marketing, which some individual manufacturer amply justifies because it produces profits for his factory, thus results in raising the cost of distributing a whole class of products.

VI

THE COST OF PRODUCTION AND DISTRIBUTION

The price which consumers pay for the merchandise they buy is the sum of four costs. These four costs are:

1. The cost of the raw material;
2. The cost of fabrication;
3. The cost of physical distribution, including transportation and storage through all the stages of production and distribution;
4. The cost of marketing, including
   (a) the cost of buying and selling the product by the producers of the raw material and the fabricators of it, and
   (b) the cost of buying and selling the finished product by wholesalers and retailers.

In the report on Marketing and Distribution of the Joint Commission on Agricultural Inquiry there is a discussion and an analysis of the consumer's dollar expended for corn flakes between the producer, manufacturer, wholesaler, and re-

tailer, covering the period from 1913 to 1921.[3]

While this product is not a staple, in the old significance of the term, it has very largely taken the place of staple foods, and the shift in consumption from the staple cereals which used to be sold out of the barrel, to a food specialty such as corn flakes, is one of the most significant changes which have taken place in the production and distribution of commodities during the past fifty years.

The following table is a rearrangement of the congressional committee's analysis of the consumer's dollar spent for corn flakes so as to show these four costs.

[3] Report No. 408, House of Representatives, 67th Congress, 1st Session, page 212, Table D15. Upon this table the committee report comments as follows:

"That it should cost approximately an average of 63 cents of the consumer's dollar to distribute 37 cents' worth of corn flakes, indicates a very definite need of an improvement in the processes of distribution. During the period shown in above chart, the producer received from his corn in his local market an average of 22.1 cents out of the dollar which the ultimate consumer paid for the corn manufactured into corn flakes. The service of transporting, grading, handling, and selling to the manufacturer costs on the average approximately 7.5 cents. In 1921 the manufacturers had reduced the cost of advertising and selling to 11.8 cents out of the dollar the consumer paid for corn flakes, in comparison with an expenditure of 16.7 cents in 1916 and 21.3 cents in 1913 for the same purpose. It seems quite probable that an increased turnover of corn flakes on the part of the wholesale grocer and the retail grocer could materially reduce their operating expenses. The wholesaler in 1921 absorbed a loss of 0.4 cents and his operating cost was 8.3 cents. The retail grocer handled corn flakes at an operating cost of 13.3 cents and received out of the dollar in sales of corn flakes 6 cents profit. The manufacturer's profit of 8.3 cents out of the dollar the consumer paid for corn flakes seems disproportionate to the wholesaler's loss of 0.4 cents and the retailer's profit of 6 cents."

TABLE IV

Analysis of Consumer's Dollar Spent for Corn Flakes

	Analysis of Com. on Agric. Inquiry	Rearrangement				
		Production		Distribution		
					Marketing	
		Basic Prod.	Fabrication	Physical Dist.	Mfr.	Wholesaler & Retailer
Producer received	21.0	21.0	.....	.....	.....	.....
Transportation	5.9	...	.....	5.9	.....	.....
Elevator margin and profit	1.6	...	.....	1.6	.....	.....
Manufacturer:						
Cost of manufacture	8.1	...	8.1	.....	.....	.....
Manufacturer's cost of selling	7.3	...	.....	.....	7.3	.....
Advertising	4.5	...	.....	.....	4.5	.....
Transportation	9.1	...	.....	9.1	.....	.....
Taxes	7.0	...	1.96	2.17	2.87	.....
Profit	8.3	...	2.324	2.573	3.403	.....
Wholesaler:						
Net margin	7.5	...	.....	5.27	.....	2.63
Loss	.4	...	.....			
Retailer:						
Operating expense ..	13.3	...	.....	6.384	.....	6.916
Profit	6.0	...	.....	2.88	.....	3.12
	100.0	21.0	12.384	35.877	18.073	12.666

Plate IV-A is a graphic presentation of this analysis of the consumer's dollar spent for corn flakes.

The report of the Commission on Agricultural Inquiry (which contains, I believe, the most authoritative figures published with regard to the proportion of the consumer's dollar paid to the raw materials producer, manufacturer, wholesaler, retailer), contains figures covering a considerable number of products in addition to the

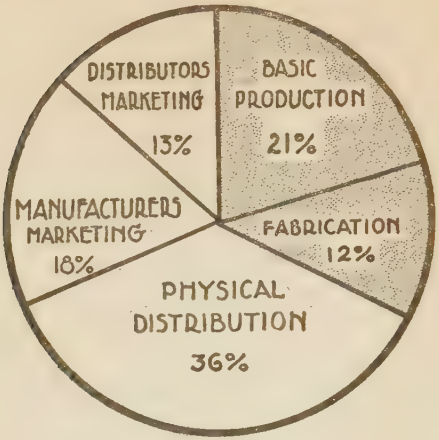


PLATE IV-A

Analysis of Consumer's Dollar Spent for Corn Flakes

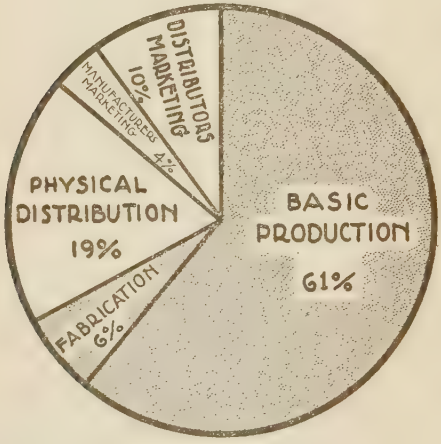


PLATE IV-B

Analysis of Consumer's Dollar Spent for Fresh Beef

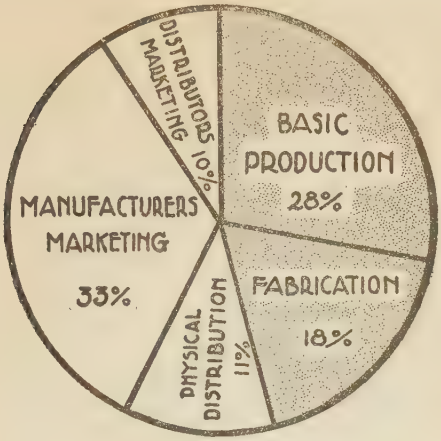


PLATE IV-C
Analysis of Consumer's Dollar Spent for Bread

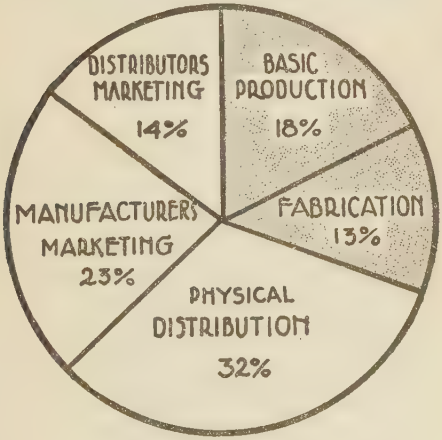


PLATE IV-D
Analysis of Consumer's Dollar Spent for Rolled Oats

corn flakes. Some of these products show higher distribution costs and some of them lower than corn flakes. But all of them reveal the large amount which the consumer paid for physical distribution, and the surprisingly large amount paid the manufacturer, rather than the so-called middlemen—the wholesaler and retailer, for marketing the products. The three products concerning which the committee's data is sufficiently complete to permit a similar rearrangement to that made of the corn flakes data, are analyzed in Table IV-A-B-C-D, and graphically shown in the corresponding plates.

TABLE IV-A-B-C-D

Analysis of Consumer's Dollar Spent for Corn Flakes, Fresh Beef, Bread and Rolled Oats

	Corn Flakes	Fresh Beef	Bread	Rolled Oats
Production:				
Basic Production	.21	.61	.28	.18
Fabrication	.12	.06	.18	.13
Distribution:				
Physical Distribution	.36	.19	.11	.32
Marketing:				
Manufacturer's	.18	.04	.33	.23
Wholesaler's & Retailer's	.13	.10	.10	.14
	$1.00	$1.00	$1.00	$1.00

Table IV differs radically from other analyses of the consumer's dollar in that every physical distribution and marketing cost has been eliminated from the cost of production.

The cost of growing the corn and of converting it into corn flakes was 33.384 cents.

About one-third of the consumer's dollar was, therefore, paid for raw materials, for labor in production, and for factory expenses of all kinds, including factory overhead, and profits earned on the production of the corn flakes as distinguished from the marketing and distributing of them.

Over one-third of the consumer's dollar—35.877 cents—was paid for physical distribution. This includes not only the amount paid directly for transportation and storage, and the incidental expenses of the growers, manufacturers, wholesalers, and retailers, but also the estimated profit which was earned in the course of this work.

A little less than one-third of the consumer's dollar was paid for marketing, but the manufacturer received 18.073 cents out of this sum, while the wholesaler and retailer together received only 12.666 cents.

We have been so busy excoriating retailers and wholesalers—under the hated name of middlemen—that we have never really taken time to find out to whom the consumers of the nation actually pay their money for distribution. Isn't it something of a shock to realize that most of the money paid is for physical distribution, and that more is paid to the manufacturers for marketing this product than is paid for all their services to wholesalers and retailers combined?

The value of all merchandise distributed by retailers in 1923, according to an estimate made by

Paul H. Nystrom,[4] was approximately thirty-five billion dollars.

This estimate makes it possible to secure an appreciation of the significance of Table IV. That table presents the facts in the form of percentages, but percentages can not possibly give us an adequate appreciation of the situation thus revealed.

If we assume that the totals in Table IV represent proportions of the 35 billion dollars spent at retail, with possible variations of from 10 to 20 per cent., then the consumers paid for raw materials from $6,650,000,000 to $8,050,000,000; for fabrication from $3,850,000,000 to $5,000,000,000; for physical distribution from $11,301,500,000 to $13,790,000,000; for marketing by manufacturers from $5,670,000,000 to $6,930,000,000; and for merchandising by wholesalers and retailers from $3,990,000,000 to $4,900,000,000.

These are colossal sums. Each fraction of a per cent. saved or wasted is important. Every time improved methods of production result in a decrease of only one per cent. in prices, it means a saving of three hundred and fifty million dollars a year; every time we add an extravagance in distribution amounting to one per cent. of sales, it means an increase of three hundred and fifty million dollars in the cost of distribution. Each one

[4] *Harvard Business Review* of January, 1925, "An Estimate of the Volume of Retail Business in the United States," p. 150.

per cent. saving creates a market for three hundred and fifty million dollars' worth of consumption goods, and each one per cent. waste destroys a market of equal size.

VII

THE RISE IN THE COST OF PHYSICAL DISTRIBUTION

That more than one-third of all that consumers pay for merchandise is paid for physical distribution—for transportation, rent, and the costs incidental to the physical distribution of goods from the moment of their first production to the time and place at which they are finally consumed—is a fact which deserves consideration if for no other reason than because of its aggregate cost.

Assuming that we spent $35,000,000,000 in the year 1923 for merchandise purchased at retail, then the total amount paid that year for the physical distribution, according to Table IV, was between eleven and fourteen billion dollars.

The amount paid for transportation is the biggest single item of cost included in the public's bill for physical distribution. The amount paid to labor for work in stock rooms, shipping departments, and similar branches of physical distribution, is probably second in importance. Rent paid for warehousing, including rent for so much of the space in retail stores used for the storage of goods as distinguished from the selling of

goods, is probably next in importance. Other large payments which are properly chargeable to physical distribution, in whole or in part, include the interest and profits on the capital used during the transportation and storing of the goods, taxes, insurance, depreciation, and distribution overhead.

If present methods of distribution involve cross hauling and unnecessary transportation and require longer periods of storage than was the case fifty years ago; if multiplying of brands has resulted in merchandise stocks which are larger in size, carried for longer periods of time, and "marked down" more than in the past, then the cost of physical distribution in the aggregate might be higher today even if freight rates, rentals, and other items of expense were lower.

We may have reduced the ton-mile cost of transporting freight, but at the same time may have increased the average miles per ton shipped so as to completely wipe out the saving and to actually increase the transportation cost on each ton of merchandise we consume.

But freight rates have not been lowered. Freight rates, rentals, wages, and nearly every overhead expense have risen, and in addition, consideration of present methods of marketing will force us to the conclusion that these methods result in unnecessary transportation; unnecessary labor and storage expenditures; unnecessary in-

creases in stocks of goods; unnecessary depreciation.

Freight rates are generally recognized as important factors in the economic life of farmers and of all producers of raw materials who market their products F.O.B. the points of exchange and conversion. If the farmer's wheat is worth $2.00 per bushel F.O.B. Chicago, it makes a great difference to the farmer whether the freight from his shipping point to Chicago is twenty cents or thirty cents per bushel. The higher the freight rate, the less there is left out of the $2.00 for the farmer to spend. That is obvious.

But the great importance of the relationship of freight costs to consumer prices is not generally recognized. The fact, for instance, that the amount paid by the retailer for freight for a single suit of clothes is obviously too small to play an important rôle in the dramatic rise in the cost of distribution is responsible for the neglect of this factor in distribution. As a matter of fact, the freight paid on a suit of clothes on its final movement from the manufacturer to the retailer is the smallest item which must be charged to the cost of transporting it.

According to the Joint Commission of Agricultural Inquiry, the buyer of clothing pays seven distinct transportation charges on the wool used in the suit of clothes in the course of its movement from the sheep's back to the ultimate consumer. Many of these payments for freight are

made on the wool before it is fabricated into the suit which the consumer buys. The early freight payments are pyramided four or five times before all the freight payments are finally "frozen" into the suit by the clothing manufacturer and the retailer and then passed on with the retailer's final mark-up to the ultimate consumer. And—as clothes happen to be one of those products which are shipped direct to the retailer by the manufacturer—and so are not transshipped from a wholesaler to the retailer—it is probable that men's clothing carries fewer freight charges than products which are handled by jobbers.

This process of pyramiding which multiplies every cost, necessary and unnecessary which enters into production and distribution prior to the time goods reach the retailer, is a phenomenon which it is important to fully understand. Freight rates are important in themselves, but pyramiding makes them doubly and trebly important.

All the factors in distribution "mark up" the goods passing through their hands by a percentage which covers their cost of doing business and the profit which it is customary to make in their line.

The average retail grocer pays out for help, rent, delivery, and other items of expense, from eighteen to twenty per cent. of the volume of his sales. He must therefore mark up what he buys at least twenty-five per cent. on his cost price in order to receive a price which will cover his ex-

penses and yield him a return upon his investment.

What is true of the retailer, is true of every factor in distribution. Each one secures a mark up on the goods passing through his hands. Each factor's mark up is a percentage of the price paid for the goods sufficient to cover his cost of doing business and the profit which it is customary to make in his line. This is true even in the case of merchants buying and selling raw materials at prices which are made on exchanges and definite markets like the cotton exchange, the wheat pit, and the wool auctions. The price at which they buy and the price at which they subsequently resell may be fixed by forces beyond these merchants' control. And yet they secure what is the economic equivalent of the retailer's mark-up because of the difference between the market prices in their primary and in their secondary markets.

What is the genesis of the mark-up? Why does the average grocer use a mark-up of 25 per cent.; the average shoe dealer and the average hardware dealer, a mark-up of 40 per cent.; the average druggist and clothier, a mark-up of 50 per cent.; and the average furniture dealer and the average jeweler a mark-up of 100 per cent.? Because there is a normal cost of business for each factor in distribution and for each type of distributor. This cost, plus whatever net profit is necessary to attract the number of factors needed to do

the work, determines the average difference between prices in primary and secondary markets.

Mark-ups by retailers, as for example by grocers, and by each factor in the process of distribution—elevators, millers, wholesalers, retailers—deviate only slightly from the normal average mark-up in each line.

Why? Because (between the upper mill stone of competition and the nether mill stone of cost-of-doing-business), each individual factor is forced, under penalty of failure, to operate upon a margin not very different from that which general experience has shown as necessary in his line.

Eliminating an independent factor by integrating distribution does not eliminate his cost of doing business, and in very few cases does it eliminate the factor's profit.

The department store which eliminates the dry goods jobber and buys direct from manufacturers is not enabled thereby to deduct the jobber's margin from the price of the goods it sells. The difference between the price at which it buys direct and the price at which it sells to the consumer is substantially the same as the combined margins of the jobber and the small retailer.

The shoe manufacturer who opens his own retail stores does not eliminate the independent retailer's and the independent jobber's margins as long as he sells his shoes at prevailing retail prices.

The supertrust which produces the raw mate-

rial, fabricates and sells it to the ultimate consumer does not eliminate any of these margins because it has no reason for selling below the market.

As long as there is free competition in the sale of any commodity and prices on the bulk of it are established in free markets, the process of pyramiding will result in passing on to consumers all freight or other costs plus progressive accretions, which in the aggregate adds enormous sums to any wastes in production or distribution.

Pyramiding makes each dollar added to the price of a product early in the process of distribution more important than any dollar added in the later stages. An unnecessary dollar of cost in the production of raw materials, or in the transportation of the raw materials before they are fabricated, will cost the ultimate consumer much more than a dollar for unnecessary expenses added by retailers, because the dollar added by the retailers is not pyramided by a subsequent mark-up, whereas the unnecessary dollar added in the early stages of distribution is marked up by each middleman through whose hands the product afterwards passes. The greater the number of mark-ups in the distribution of a product, the greater is the importance of eliminating waste early in the process of distributing it.

The tremendous importance of the pyramiding of transportation costs is made clear by Table V, which shows how the mark-ups progressively in-

crease the transportation cost before it is finally fixed in the price which the consumer pays the retailer.

TABLE V *

Pyramiding of Transportation Costs

	Mark-up on Cost	Transportation Between Farmer and Elevator	Transportation Between Manufacturer and Wholesaler	Price at Each Stage of Distribution
	per cent	*cents*	*cents*	
Transportation Costs .		5.9		$0.269
Elevator Mark-up	6	6.254		0.285
Manufacturer's Mark-up	155	15.947	9.1	0.728
Wholesaler's Mark-up.	10.8	17.669	10.08	0.807
Retailer's Mark-up....	23.9	21.891	12.49	1.00
Cost to Consumer.....		34.38 cents		

* Table showing total cost to consumer for transportation of one dollar's worth of corn flakes from farm to elevator and from factory to wholesaler, based upon an analysis of figures in the report on "Marketing and Distribution" by the Commission on Agricultural Inquiry.

Table V shows that the 5.9 cents, which it cost to transport a dollar's worth of corn flakes between the farmer and the elevator, pyramided to 21.891 cents by the time the consumer paid for it, while the 9.1 cents, which it cost to transport them between the manufacturer and the wholesaler, pyramided to 12.49 cents. The actual sum paid for transportation amounted to only 15 cents, but the mark-ups by the various factors involved added 19.381 cents to that sum, making the total cost of transportation for which the consumer paid 34.38 cents.

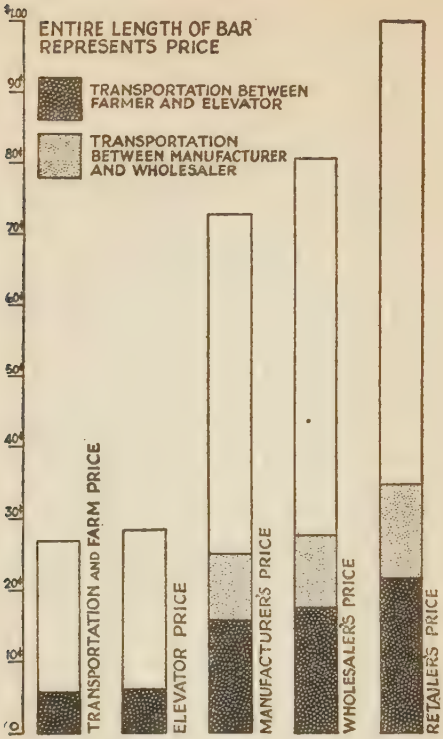


PLATE V

Pyramiding of Transportation Costs at Each Stage of Distribution

Increases in freight rates assume a new importance when viewed in the light of this phenomenon. Under modern conditions goods are shipped and reshipped so often in the course of production and distribution that any general increase in freight rates is certain to increase the level of prices to a much greater extent than is recognized.

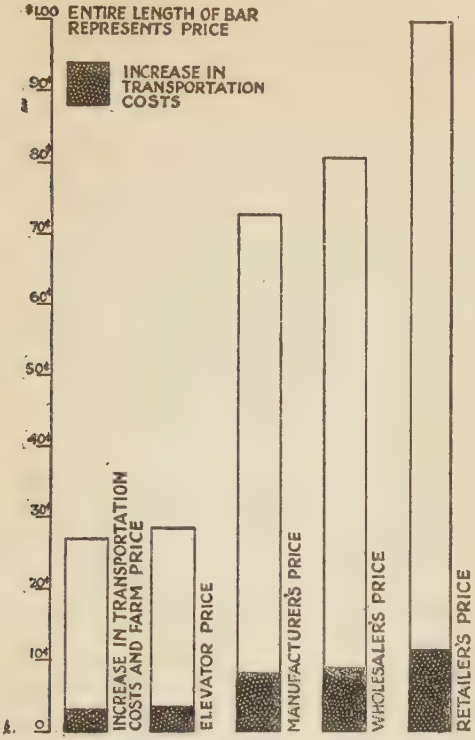


PLATE VI

Pyramiding of Increase in Freight Rates at Each Stage of Distribution

The really serious aspect of the various increases in freight rates since 1913 is evident from a study of Table VI.

In 1913, the cost of transporting one dollar's worth of corn flakes from the farm to the elevator was 2.9 cents. By 1921, the cost of transportation

had increased to 5.9 cents. The cost of transportation at this early step in the distribution of corn flakes increased three cents in eight years. As this increase in the cost of transportation was pyramided by each of the factors subsequently involved in the distribution of the corn flakes, it was passed on to the consumer not at the original three cents but at an increasing progression, varying with the margins upon which the various factors involved operate their businesses, until it amounted to over eleven cents. This is graphically shown by Plate VI.

TABLE VI *

Pyramiding of Increase in Freight Rates

	Mark-Up on Cost	Increase in Transportation Costs	Price at Each Stage
	Per Cent		
Increase in Transportation Costs, 1913 to 1921		$0.03	$0.269
Elevator Mark-Up	6	0.0318	0.285
Manufacturer's Mark-Up	155	0.0811	0.728
Wholesaler's Mark-Up	10.8	0.08986	0.807
Retailer's Mark-Up	23.9	0.1113	1.00
Cost to Consumer		$0.1113	

* Table showing cost of consumer of increase in transportation costs on one dollar's worth of corn flakes.

It will be seen that the increase of three cents in the transportation cost at the very beginning of the process of distribution, after four mark-ups, actually resulted in the consumers paying over eleven cents when buying corn flakes—nearly four times the amount of the increase.

We are thus brought face to face with the startling fact that on an article of such wide spread consumption as corn flakes, the consumer paid for this increase in transportation charges more than 50 per cent. of the total amount he paid to the retailers for their services in supplying him with corn flakes when and where he desired them.

In order to save consumers a sum equivalent to what they paid for that increase in transportation costs, wholesalers would have to carry on business for nothing and in addition lose nearly three cents—rather a high price to ask them to pay for the privilege of handling a dollar's worth of corn flakes. Or retailers would have to cut their entire cost of doing business, including their profits, about 60 per cent. in order to save their customers a similar sum.

Elsewhere I refer to the tendency of manufacturers to broaden their markets and to invade territory which is not naturally that in which the manufacturer can market his product most economically. Theoretically, the lower unit of cost of production which is made possible by increasing the volume of sales in this way should more than offset the increased cost of marketing and the greater average distance his product is transported. The only difficulty with this theory is that it rarely works out that way in practice. If the local manufacturers, in what might be called the "foreign" territory, were quite content to leave the invading manufacturer in undisputed posses-

sion of the business in the invader's home territory, all the business which was secured in the foreign territory would tend to lower the invading manufacturer's cost of production.

If Chicago manufacturers could secure a thousand desirable outlets in New England in addition to those they supply in their own natural territory, they could probably lower their cost of production sufficiently so as to quote prices F.O.B. New England in full competition with Boston. If, however, the Boston manufacturers at the same time secure one thousand desirable outlets in the Chicago manufacturer's territory, isn't the net return a mere exchange of accounts between the two groups of manufacturers? Both groups after the invasion of each other's territory travel their salesmen and ship goods more than a thousand miles more than before. Every distribution cost in consequence is raised, and the higher costs are applied not only to the sales in the distant markets, but also to the sales in the local market which have not contributed to the higher selling costs.

The net effect of the present day fight among manufacturers for the national market is to increase enormously unnecessary transportation of merchandise and to greatly increase expenditures for selling, since salesmen and advertising costs increase enormously as they work further and further from their home territory. Yet as a rule we are so dazzled by the spectacular economies of mass production, that we refuse to face the fact

that marketing extravagances in many industries eat up all that mass production saves.

It has always seemed absurd to me that Kansas farmers should ship wheat to Minneapolis, and then have flour shipped all the way back from Minneapolis to Kansas. Local mills, even though it costs a trifle more for them to make flour than it does the mass producers, are able to save considerable sums out of the differential which freight alone gives them. Yet in the milling of flour—which lends itself so admirably to local production—we have drifted into a state of affairs where ten of the national mills are able to supply fifty per cent. of the consumption of the country.

The crowning absurdity seems to me the shipping of Oregon apples across the continent to supply the New York market—a market which is supplied with as luscious fruit by local producers, but which pays a premium for Oregon apples—well, because the Oregon producers are better advertisers than the New York growers. This is a thing which is easy to understand, but impossible for an intelligent people to justify.

A monograph dealing with the marketing of live stock and meat issued by Armour's Live Stock Bureau, Chicago, Illinois, contains four maps which illustrate very graphically the tendency of commodities to carry a greater burden of transportation costs today than was the case previously.

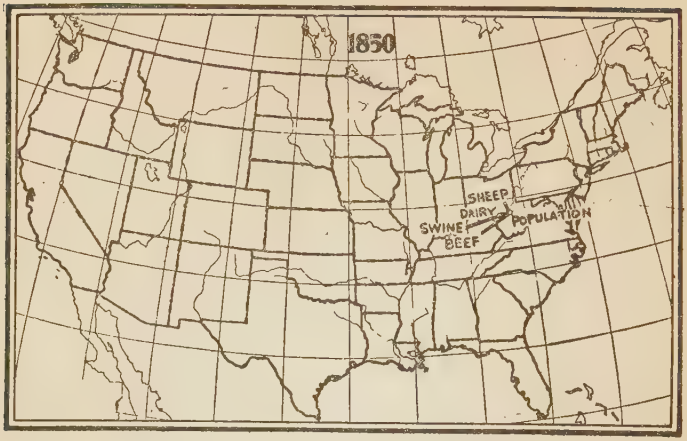


PLATE VII-A

Centers of Human and Livestock Populations—1850

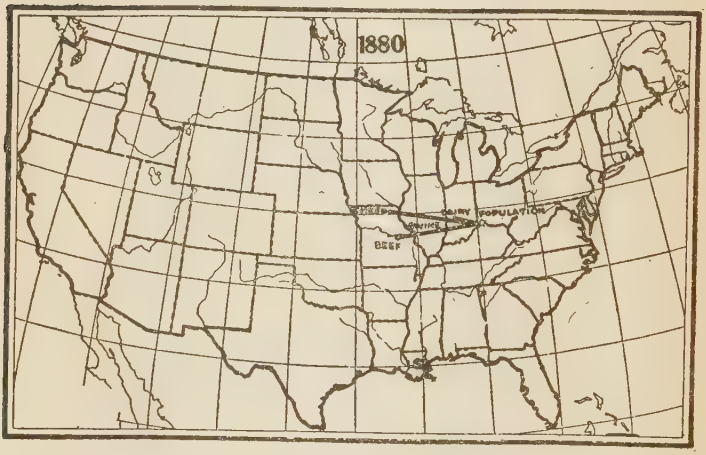


PLATE VII-B

Centers of Human and Livestock Populations—1880

The map of 1850 shows the distance between the center of population and the centers of production of dairy products, sheep, swine, and beef. The map of 1880 shows how considerably the distance between these centers had increased in thirty years, and the subsequent maps for 1910 and 1920 show how enormously greater is the distance most of these commodities are being moved today.

In the case of the products of the meat packing industry this increased distance which the meats can be shipped is both a cause and a consequence of the development of elaborate refrigerating shipping systems. The development of the refrigerator car made it possible to ship fresh meats great distances. In turn, the possibility of shipping from Chicago enabled the great meat packers to undersell the local meat packers section by section. As a result, we now have the absurd system whereby the raw products of an industry, in this case the live stock, are shipped great distances to the meat packing centers and then, after being slaughtered, shipped equally great distances back to the point of origin.

There is apparently a greater justification for stupidly long hauls in the case of live stock itself than in the case of many other products, because the less sparsely populated sections produce the raw material of the meat industry—live stock—more economically than it can be raised in the densely populated sections. The justification for

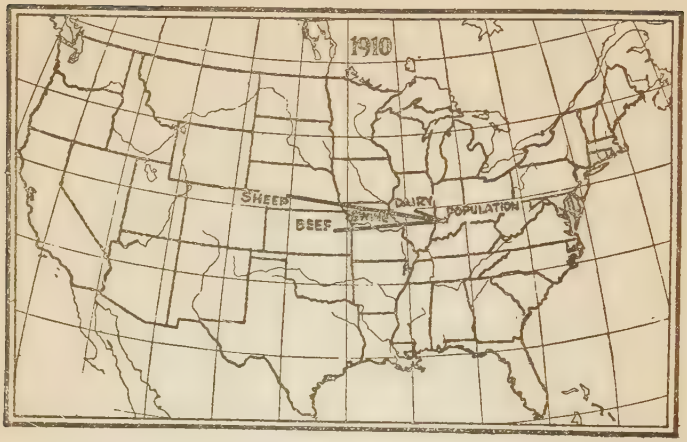


PLATE VII-C
Centers of Human and Livestock Populations—1910

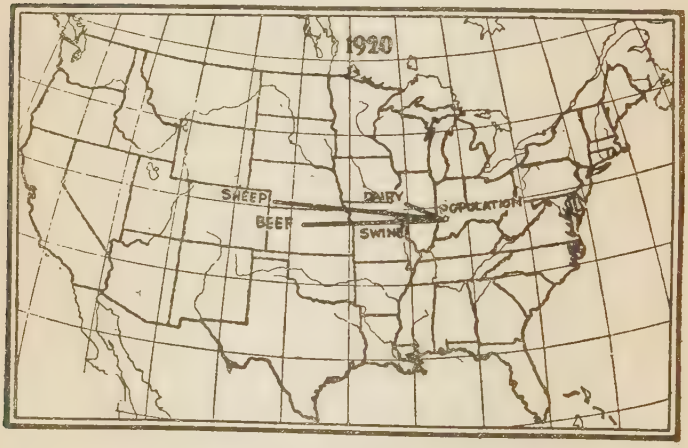


PLATE VII-D
Centers of Human and Livestock Populations—1920

it, however, would undoubtedly be wiped out if the relationship of terminal costs to long distance hauls were changed. There are good grounds for believing that terminal charges are disproportionately high. If the railroads of the country were to give to the problem of reducing terminal costs one-half the attention which they give to the problem of carrying long trains of cars long distances economically, there is little doubt that livestock could be produced near the centers of population at a saving over the combined low cost of production in sparse sections and long distance hauls from them.

When it comes to products the manufacture of which can be carried on equally economically in many sections, the uneconomic national marketing of the products made inevitable by our present system of freight rates is an absurdity for which manufacturers, retailers, and consumers all pay in the long run.

A single change in our basis of proportioning terminal charges and carrying charges, even though the national bill for freight was not reduced, would tend to reverse this process of centralization. Lower rates for short hauls and higher rates for long hauls would give local manufacturing a chance to exist, and by the same token, centralized manufacturing would cease to receive the subsidy by drawback which helps it to overcome its inherent disadvantages of distance and location.

VIII

THE RISE IN THE COST OF MARKETING

Out of every dollar spent by the consumer for corn flakes in 1921, only 12 2-3 cents was paid to cover the charge of merchandising by wholesale and retail grocers combined. Out of the same dollar, however, a little over 18 cents was paid to cover the charge of the manufacturer for marketing.

The manufacturer's charge was about 50 per cent. greater than the combined charge of the so-called distributors. This is a startling fact. It is true that it is not yet universally a fact concerning everything consumers buy. There are still a considerable number of products which are being economically marketed by the manufacturers. But the whole tendency of the times is toward a reduction in their numbers. The methods which were originally used to exploit patent medicines, alcoholic beverages, and cigars and cigarettes are being year by year applied to more and more of our staple commodities; to the bulk of the products purchased at retail and to a considerable part of those purchased for industrial uses.

Most of the staple groceries—flour, sugar, coffee, soap, canned and bottled goods; many of our staple meat products—ham and lard; nearly all of our drugs and toilet articles; dry goods and furnishings which lend themselves to labeling and trade marketing, and all kinds of merchandise which can be packaged, are no longer marketed as staples but as specialties. Each year sees an additional number of staples converted into specialties which are marketed by the high pressure methods used by the manufacturers of corn flakes. Another twenty-five years of such changes in the control of distribution as we have experienced since 1900, and the marketing charges of nearly all manufacturers will be higher than the combined charges of the retailers and wholesalers who will sell their products.

That so much should be spent to market a grocery specialty of such wide sale as corn flakes indicates the need for careful examination of manufacturer's marketing costs.

Corn flakes are made from our leading American cereal. Fifty years ago no corn product carried such a burden of marketing expense. Corn and corn products were sold in bulk. The cost of marketing by the millers was an item so insignificant that it could hardly be measured. With the change to modern methods of selling and advertising, the manufacturers introduced nearly every one of the new and costly methods of distribution which I have called high pressure marketing.

Today corn is shipped to mills often located at great distances from growing centers, then processed, and shipped even greater distances to jobbers and retailers at the points of consumption. The corn flakes and other corn products are trademarked and packed in small, elaborately decorated cartons containing a few ounces of the actual foodstuff itself. The cartons are in turn shipped in small and comparatively expensive containers. Armies of salesmen call upon retailers and jobbers to see that they are amply stocked with their brands. Over the whole nationwide field of operations, millions of advertisements are distributed by the manufacturers. Every medium of advertising is utilized—the billboard, the newspaper, the magazine, the street car card—to persuade the consumer to eat corn flakes.

I submit in all seriousness the proposition that it is not necessary for manufacturers to advertise in order to make human beings eat. They used to eat before the national advertising of foodstuffs became one of our great national sports, and they will continue to eat even if some miracle were to efface every vestige of food advertising from the American scene. Grocers would continue to supply them with groceries, just as druggists would supply them with drugs, hardware dealers with hardware, and clothiers with clothes. The only difference would be that consumers instead of being confused by the rival claims of superiority by manufacturers would rely more

completely upon their dealers for advice and information than they do now, and manufacturers, instead of arguing their case before an audience of consumers who are amateurs in knowledge of merchandise, would have to argue their case before a better trained and more experienced audience of jobbers and retailers. Having to sell their product to the trade would tend to eliminate buncombe from manufacturer's claims. Selling would have to be on the basis of quality, price, and value. Few of the arguments about consumer demand and acceptance, which are now used by manufacturers to persuade jobbers and retailers to feature brands rather than merchandise, could survive such a regime. Manufacturers' marketing costs would inevitably shrink and the saving would represent a clear economic gain.

Let me make myself clear. In allocating the responsibility for the rise in the cost of marketing, I am placing major responsibility upon the manufacturers of the country and minor responsibility upon the wholesalers and retailers. Indeed, I am sometimes tempted to absolve the distributors entirely and hesitate only because they also are infected with the mania for sheer volume of sales, and indulge in extravagances of merchandising for which there is no necessity. Price competition, however, sets sharp limitation upon such extravagances among jobbers and retailers.

I base my statement as to the major responsi-

bility of the manufacturers for this state of affairs on two self-evident propositions:

1. That manufacturers are under an apparently inescapable pressure to extend their markets and that the capitalization of the goodwill created by the demand for their trade-marks enables them to shift the high cost of marketing to wholesalers, retailers, and the general public.

2. That the vast majority of wholesalers and retailers are under no essential compulsion to indulge in merchandising wastes, and that price competition prevents those who do indulge in such extravagances from passing the cost on to the public.

It is not necessary in order to establish these two propositions to furnish evidence that in many industries the manufacturers are spending more for marketing than are the wholesalers and retailers.

I have cited one industry out of many of those studied by the Commission on Agricultural Inquiry. The report of the Commission furnishes other cases. But even if the manufacturers spent less than the so-called distributors, what they do spend has a much greater importance because their extravagances are pyramided while the retailers' are not.

In the very nature of things, retailers and jobbers are passive factors in the distribution of the products in their line. They are suppliers of the various commodities and of the various

brands of each commodity they handle to their customers.

The retail grocer's real unit of sales, for instance, is not units of a product sold, but numbers of customers who buy their groceries from him. His biggest asset is not the fact that he sells many cases of soap or bags of flour, but the fact that he has many regular customers who buy all kinds of groceries from him. Eighty to ninety per cent. of the entire trade of retailers consists of sales to regular customers. It is to all intents and purposes a matter of indifference to the grocer just what product or just what brand a customer buys from day to day, since in the course of time he will supply to each customer all the various items which the customer uses. The retailer exists because he supplies the demand for groceries, not because he creates a demand for individual items like corn flakes. He gets the proportion of their income which his customers spend for groceries as long as he remains their grocer.

If stocking mayonnaise will please and help to hold his customers, or tend to secure new ones for him, he will add a line of it to his stock. If it fails in this regard, he will drop it.

If featuring the Pink Violet brand helps him to hold and to build trade, he will push that brand for "all it is worth."

But if the brand fails to build trade, he may not only cease to feature it—he may drop it from his

stock entirely or even replace it with another commodity.

Manufacturers, on the other hand, are active factors in the distribution of the particular commodities which they manufacture. The mayonnaise manufacturers can not rest content with the fact that consumers eat. They must make them eat mayonnaise. It is to the interest of each individual manufacturer to stimulate the consumption of mayonnaise generally, but above all the consumption of his particular brand. The individual manufacturers in every industry are engaged actively in enlarging the market for the production of their own factories at the expense of the production of their competitors, while their industry as a whole is actively engaged in enlarging the market for its product at the expense of the market of competing industries.

Clothing manufacturer competes with clothing manufacturer, but the clothing industry as a whole is engaged in competing with all the automobile, the radio, and the furniture industries. If the consumer diverts a considerable portion of his income to a new product such as radios or phonographs or automobiles, of necessity the consumer's expenditure for clothing is in some proportion lessened. The entrance of new industries into the arena of production intensifies the marketing problem of all industries.

It is the competition between manufacturers, both inside each industry and between industries,

which furnishes the fertile soil in which high pressure selling, advertising, and marketing flourish.

The manufacturer of a grocery specialty, anxious to operate his plant to its full capacity, and resentful of the indifference of jobbers, puts crew after crew of canvassers, demonstrators, and specialty salesmen in the field, increases his advertising appropriation, and literally "forces" his product into distribution.

A manufacturer of shoes, dissatisfied with the volume he is able to secure from sales to established retailers, eliminates the retailer from consideration in territory where his sales are insufficient, and opens chains of shoe stores to insure adequate distribution for the productive capacity of his factory.

A manufacturer of brooms and brushes, anxious to extend his business, finds jobbers and retailers well supplied with such products, so he cuts clear across the normal channels of distribution—starts an immense advertising campaign using double page spreads in colors in magazines circulating by the millions, hires an army of house to house canvassers, and lo, his product is being distributed!

What is the effect both upon business and upon consumption of this high pressure marketing?

The corn flakes furnish a particularly flagrant illustration. Here is a foodstuff consumed by millions of people yearly, and made from a cereal which has been an item in the diet of the country

since its settlement. Marketed as it is today, 21c worth of corn, in the form of corn flakes, costs the consumer one dollar.

The high pressure method of selling this cereal results in jobbers and retailers carrying many brands. Carrying many brands means larger stocks of corn flakes than are really needed to meet the desires of their customers for this particular product. The turnover of both wholesalers and retailers is reduced; deterioration of stocks is increased, but what is even worse, prices are raised and consumption, instead of being stimulated, is reduced.

If it be objected that corn flakes represent an extreme case—that I should use an average case rather than a flagrant one—I can only say that, flagrant as it is, it is already typical. If I really wanted to cite an extreme case, I would cite the case of bran, which one advertising trade paper boasted, costs $20 per ton, and is being sold to consumers for $1,000. When I think of that sublime example of modern marketing magic, I am astonished at my moderation in calling attention to a case in which 21 cents worth of corn is sold to the consumer for $1.00.

Fifty years ago there was scarcely a single section of the country which did not have its own flour mill, its own iron forge, its own saw mill, its own tanneries, and its own manufacturing establishments of various kinds. Nothing was brought from a distant point of manufacture which it was

possible to produce near at home. The cereals which were ground in the local mills were home grown. The lumber, the hides, the iron, the fuel used in these local industries were principally neighborhood products.

Today one can find the remains of these old industrial establishments in almost every section of the country which was well populated during the Civil War. There are numberless mills fallen into ruin, abandoned forges, even abandoned mines—mines which were operated as long as there was a local market for the minerals extracted from them, but which were abandoned because they could not be profitably operated when it became necessary to ship ores to distant forges and mills.

Statistics furnish only a faint record of this transformation.

The census of 1870 lists 252,148 manufacturing establishments. The population at that time was 38,558,371. This means that there was one manufacturing establishment for every 152.9 persons.

In 1920, the number of establishments was 290,105—an increase in the number of establishments of only 37,957. In the meantime, population had grown to 105,710,620, making the average number of persons to each establishment 364.4.

It is evident that the change from local manufacturing (and therefore local distribution) to distant manufacturing (and national distribution) is reflected in the relative reduction in the number of factories.

However, these figures do not adequately convey the transformation which has taken place, principally because they make no allowance for concentration of production within each industry. In many of the industries, especially those which lend themselves readily to high pressure marketing, a comparatively few manufacturers supplying a national market produce more than all the other manufacturers combined.

According to Hotchkiss and Franken,[1] L. E. Waterman Company does 85% of the fountain pen business of the country. Wm. Wrigley Jr. Company does 70% of the gum business of the country. Eastman Kodak Company does almost the entire business of the country in cameras and films. Colgate and Company does around 60% of the tooth paste business. Mint Products Company, Inc., makers of candy, do 75% of the business in their product. Proctor & Gamble Company, makers of "Crisco," do almost 60% of the business in this product. O'Sullivan Rubber Company estimates that nine out of every ten rubber heels affixed to shoes by dealers are O'Sullivan.

There are several hundred factories producing crackers and biscuits, yet two of them practically dominate cracker and biscuit production. According to Frederick Beers, Manager of production for the National Biscuit Company, that company does the following proportions of the total business in its lines in the country:

[1] "The Leadership of Advertised Brands," 1923.

Year	Sales	Per Cent of Total U. S. Business
1914	46,143,210	51
1919	101,707,597	49.9
1921	104,536,255	55.7

As the Loose-Wiles Company, which is the second largest biscuit and cracker manufacturer of the country, does from 15% to 20% of the total business, these two manufacturers do about 75% of the total business in this line.[2]

All these concerns do a national business and cultivate the national market.

The period in which larger and more economically operated factories have replaced smaller and more expensively operated factories is a part of the story of the industrial development of the country full of fascinating history. The new large factories were able to undersell and outsell the old small factories—sometimes in fair and open competition by furnishing a superior product, or the same product at a lower price, or by using those methods of high pressure marketing in which we are interested, but sometimes the supremacy of the larger factories was unfairly won by cutting prices section by section until one local factory after another was ruined. The national enterprises were able to survive the losses in territory in which there were local competitors because they could recoup their losses on sales in other sections.

One fact of great importance which emerges in

[2] *Printers' Ink,* December 20, 1923.

connection with the disappearance of these local manufacturing enterprises and their replacement by larger factories is this: the local enterprises had no complex problem of distribution. They could rely upon the simple distribution methods needed to supply the territory in which they were located and in which they could operate economically. But the great factories which today have taken their place have naturally very complex problems of distribution. As factory production moved further and further from the points of consumption, distribution machinery had to be developed to cope with the new conditions.

The question is, have the higher costs of the methods of distribution necessary under the new system eaten up the economies in mass production which modern methods make possible?

Concerning a great many lines of production, I think this question would have to be answered in the affirmative. What has been saved by lowering the cost of production and fabrication has been lost in unnecessary and wasteful transportation and extravagant marketing. Out of the enormous quantities of commodities which science and art makes it possible for us to secure from our farms and factories, we produce and consume but a very small part, because of foolish systems of distribution. We utilize so little of our potential production principally because we have never fairly faced the problem of distributing economically all that it is possible for us to produce.

IX

THE RISE IN THE COST OF MERCHANDISING BY RETAILERS AND JOBBERS

Before dismissing this question of responsibility, it is necessary to consider to what extent modern wholesaling and retailing may have contributed to the rise in the cost of distribution.

It is difficult to say whether the price we pay for wholesaling and retailing is considerably higher today than fifty years ago because there is no phase of our economic life concerning which we know less. We do know, of course, that the numbers of persons engaged in retailing have risen year after year; that the total number of retail stores has risen, and that the number of retail stores per capita is greater today than fifty years ago. As to wholesaling, even less can be said with certainty. In the absence of any census of distribution and of any statistics as to the number of retailers and jobbers today and in years gone by; the volumes of their business and their costs of operation, the student of this subject has to be satisfied with generalizations based upon matters of common knowledge.

This being the case, if we are to come to some

conclusion as to the part which retailers and wholesalers may have played in the rise in the cost of distribution, we must look to the broad, underlying operations of distributors and determine from them whether or not modern retailing and wholesaling tends to increase the cost of distribution.

The fact that wholesalers and retailers are primarily creators of time and place utilities, while manufacturers are primarily creators of basic and form utilities, is the cause of a significant difference between them and the manufacturers.

Consumers may not consciously say it to themselves, but in effect they ask two questions of every retailer to whom they give their custom. The first is, "Does this retailer carry what I like or want?" The second is, "Has he the things I desire when I am in the market for them?" Both these questions presuppose that the retailer and wholesaler carry a stock of goods at a place and time that suits the convenience of the customer. The nearer the place and the shorter the time in which the customer can be supplied with his needs, the easier it is for the distributor to satisfy him. The further the place and the longer the time, the greater is the difficulty under which the distributor labors. As between the neighborhood store and the distant department store, and between the village general store and the Chicago mail order house, so great is the advantage of the store nearest to the customer in place and time, that it

is necessary for the department store or mail order house to show extraordinary savings and carry very much larger varieties of merchandise in order to secure and hold their customers. The desire of the consumer to go to a place which is convenient and to get the merchandise immediately he wants it, is the basic reason for the existence of the independent retail store. The further retailers and wholesalers are located from the vicinity of their customers, the greater is their cost of serving and holding them.

From this it should follow that most of our retailers and wholesalers would have to operate in limited territories. This is actually the situation. The overwhelming majority of our city retailers draw their trade from a distance of a few blocks from their store. Nearly all our country retailers draw from larger but still definite circles covering a territory some miles from their stores. Department stores and large specialty stores draw from still larger circles. These are, however, very sharply circumscribed by their delivery services. The fact that retailers and wholesalers generally operate in restricted territories is the principal reason why I have come to the conclusion that they are not fundamentally responsible for the rise in the cost of distribution.

The maximum amount of business of the retailers in any community is, broadly speaking, limited to the total expenditure of those who reside in that community. Competition between

retailers can only result in transferring the purchasing power existing in their territory at any given time from one retailer to another. While one retailer may be able to increase the volume of his business at the expense of competitors, either by selling at lower prices, or giving his customers better service, all the retailers together can not sell more than the residents in that community earn.

No amount of competition among retailers can increase the total consumption buying in a community unless the community as a whole increases its income or reduces the proportion of its income which it usually saves. By wiping out savings accounts, and bank deposits, and checking investments in stocks and bonds, sales of goods for consumption could be temporarily stimulated, but the period of increased sales would continue for so short a time that it would hardly increase total sales over a period of a single year.

It is true that competition between retailers, especially in some of the larger cities, has resulted in extravagant expenditures for advertising, display, and similar efforts to win trade. Yet it is extremely doubtful whether the payment of the public for retailing has materially been increased by it. Competition among retailers is so intense that neither individual retailers nor communities of retailers can increase prices arbitrarily. If the retailers in any one community indulge in extravagant and wasteful merchandising and at-

tempt to cover it up by charging higher prices, business simply moves out of town, or the higher local prices invite enterprising merchants to open new stores, which would for a time take advantage of the higher margins for profit prevailing in that town, but which would ultimately bring all prices down again.

When some misguided retailer tries to increase the volume of his sales by extravagant advertising, display, and salesmanship generally, he very quickly finds that while his extravagance can be continued up to the point at which he has used up his margin of net profit, it can not long be continued beyond that point *because he cannot increase his prices to cover.* Competition in retailing and wholesaling is still fundamentally a question of price. Even the so-called quality stores have to meet price competition on higher levels.

This is the nub of the situation. The retailer cannot indulge in distribution extravagances and survive because the price at which he sells is a competitive price. The most efficient retailer sets the price, and the retailer who indulges in extravagant merchandising must cover the cost of it out of his net profits.

This is the reason why retailers' margins have changed so little over a considerable period of time. For nearly fifty years, the mark-up of the retail grocer has been around twenty-five per cent; that of the dry goods dealer around forty per cent; that of the clothier around fifty per cent;

and that of the furniture dealer around 100 per cent. In recent years, as manufacturers have taken on more and more of the function of merchandising, retail margins have been contracting. This is most apparent in the grocery field, in which the retailer and wholesaler have steadily shrunk in relative importance to the manufacturer, with the result that margins on many items in the line of groceries yield the distributors less than the cost of doing business.

Just as competition regulates retail and wholesale margins, it should regulate manufacturing margins. Just as it prevents extravagant merchandising among the distributors of the nation, it should prevent extravagant marketing among the manufacturers of the nation. Just as it checks undue transportation by retailers and wholesalers, it should check unnecessary transportation by manufacturers.

But competition has apparently failed in many cases to regulate the distribution practices of some of our largest manufacturers. As we shall see, during the past fifty years, manufacturers have increasingly indulged in those methods of high pressure marketing to which I ascribe so much of the responsibility for the rise in the cost of distribution. With apparent impunity, they have added to the price of their products the cost of extensive selling and advertising campaigns and the cost of shipping to distant territories. They have evidently discovered a mechanism

which enables them to lift their products outside of ordinary competition and to hide the fact that they are not giving to the consumers of the nation the benefit of those lower prices to which the general progress in production entitles them.

Before I finish, I shall show what this mechanism is, why it came into existence, and how a determined effort to establish a less extravagant machinery of distribution would enormously increase the prosperity of the rank and file of manufacturers, wholesalers, and retailers, and add to the well-being and happiness of the consumers of the nation.

PART II

MARKETING A LA MODE

X

HIGH PRESSURE MARKETING

In 1865, during that period of our industrial era when the demand for manufactured products far exceeded the capacity of the factories to supply it, a partnership under the name of the Moline Plow Company began the manufacture of a line of plows. The first plant of the company consisted of a small frame building. The company prospered from the start. In 1871 it was incorporated. Its profits were amazing. For a long period the dividends to stockholders amounted to 20 per cent a year.

During the early years of the company's history its principal problem was of the same general character as that of most manufacturers of that period. The owners concerned themselves almost exclusively with the work of manufacturing a line of plows by the most efficient methods which the existing state of industry made possible. The marketing of their plows was a comparatively simple process, and the entire "marketing problem" was disposed of by operating on the theory that so long as they produced satisfactory plows at a low enough price to meet all competition, the

market for their plows would grow as rapidly as they were able to increase their facilities for manufacturing them.

Then came the era of high pressure marketing; the period, now at its zenith, when selling and advertising and distribution methods sacrifice the general economy of distribution of the products of an industry to the aggrandizemnet of the individual manufacturer.

The Moline Plow Company, which had been originally an organization for the production of plows and tillage implements, gradually changed from primarily a *producing* organization to primarily a *marketing* organization.

In implement manufacturing, high pressure marketing took the form of expansion by the manufacturer so as to sell through one selling organization and under one trade name a full line of agricultural implements. The leading manufacturers in the field set the pace for expansion of all the manufacturers by selling not only the particular implements which they were organized to produce, but full lines of farm implements of all kinds.

The Moline Plow Company followed the trend of the times with an ambitious program of expansion. A factory at Poughkeepsie, New York, was bought; another was acquired near Minneapolis; a third in Freeport, Illinois; and so on. It was no longer a plow company, but a distributing agency

for wagons, tractors, and even automobiles, all of which were marketed under the Moline name.

P. H. Noland, General Sales Manager of the Moline Implement Company, which is now carrying on the business, describes [1] in considerable detail the methods which were used during the era of high pressure marketing by the company.

"The old way," he says in speaking of the methods which were and still are in general use in the marketing of agricultural implements, "was to work through branch houses, each of which maintained an expensive staff of accountants, shippers, laborers, salesmen, canvassers, and collectors; to extend extraordinary long terms; to make the dealers practically agents and to add to an already heavy load almost every 'service' that ingenious minds could think of to attract business—*except the fundamental service of economical marketing!* Manufacturers had salesmen who called on dealers; canvassers who went out and drummed up business for dealers; experts who helped to install implements and service them; and bill collectors who helped the merchant get his money so that the manufacturer might get his! Altogether an expensive outfit. We used to figure that only about half the time

[1] From the article in the June 3, 1925, issue of *Advertising and Selling Fortnightly*. What Mr. Noland has to say is written with such naïve disregard of its underlying significance that what he says is much more effective than anything which I might say myself concerning high pressure marketing.

of our salesmen was devoted to selling; the balance was given over to collecting.

"Long terms tied up the manufacturer's money endlessly. An implement sold in the spring was likely to be billed for fall payment; but often it was understood that if the dealer failed to dispose of the implement that season, he would not have to pay the manufacturer until the next fall. This was a survival. In the early days of the industry it was not so bad, because the West—where implements were needed—had no money and few banks, and the manufacturer by extending long terms served as a useful agent in employing the excess capital of the East for the development of the West. But the system remained after the West grew up. It entailed extensive bookkeeping, increased the risks, and resulted in extremely low rates of turnover. For the industry as a whole, the rate of turnover has probably been lower than for any other industry approaching it in size; we figure it runs somewhere between once in eighteen months to two years.

"Another survival was the excessive number of dealers. Manufacturers established agencies at every cross-roads store. When railroads were few and slow and wagon roads were bad, something of this sort had been almost essential. But with the speeding-up of transportation and communication facilities, the system began to weight down the industry with waste. The territories of dealers were so small that few of them could hope

to sell much. Their expense percentages accordingly were high. They could not buy in bulk and save money by that means. Retail prices were high. Yet the dealer got very little profit out of it.

"Finally, there was the 'free' service. Of course it was not free—it found its way into the price. It was available for all customers. Those who accepted or demanded it, got it, but at the expense of those who did not need or demand it; the latter paid for something they never received.

"This description of the old method is not overdrawn. It is what we did; what everybody did. On many lines we figured that the factory cost was not fifty per cent of the price the consumer finally paid. The rest was eaten up in distribution costs."

Are the methods of marketing described by Mr. Noland peculiar to the implement industry? No. Instead of being confined to this industry, his description might be applied almost word for word to one industry after another.

Not every industry uses all the methods Mr. Noland describes, but some of them are being used in every industry which indulges in high pressure marketing. The mania for a full line is indulged in by manufacturers who make products ranging all the way from agricultural implements to paint brushes. A manufacturer makes a paint brush; creates a demand for his brand through advertising, and soon he is selling tooth brushes, shaving

brushes, and every imaginable kind of brush under his brand, many of them not of his manufacture at all.

The mania for installment selling is a device used not merely by the manufacturers of agricultural implements and productive machinery of an enduring nature, but also by those selling automobiles, phonographs, and radio receivers, and by those selling clothing, paint, ice, and fuel, the installments on which have to be paid long after the commodities have been consumed.

The mania for house to house selling has transformed the peddler of old into the specialty salesmen of to-day. There are concerns selling from door to door articles varying from perfumery to brooms and from raincoats to silk hosiery, who employ thousands of canvassers and whose methods of operating are scientifically regulated.

It is well worth taking time to give consideration in some detail to these methods of marketing and to try to form a true picture of how extensively they have been applied to the distribution of most of the products we are now consuming. In their entirety, these methods represent a complete transformation in the marketing methods which were in general use during the period prior to the expansion of the Moline Plow Company.

In what he says concerning the period in which the Moline Plow Company was indulging in this high pressure marketing, Mr. Noland speaks merely from his own experience. Yet he re-states

the gist of my indictment of these methods of marketing in these words: "On many lines," he says, "factory cost was not 50 per cent of the price the consumer eventually paid. The rest was eaten up in distribution costs."

Before we study in some detail these methods of high pressure marketing, it may be of interest to follow the history of the Moline Plow Company and learn how the successors of the original company have managed to make a success out of a return to the methods which preceded the era of high pressure marketing. When the bottom dropped out of the farm market during the period of deflation following the war, the Moline Plow Company failed to weather the storm. Bankers took the company in hand and reorganized it. A new company was formed for the purpose of returning to the manufacturing policy of the original company.

Speaking of the decision of the successors of the company to abandon high pressure methods of marketing, Mr. Noland says:

"Now, it is not easy to buck the established practices of an entire industry with something radically different. Yet that is what we decided to do. In the new merchandising plan we worked out we included these principal features: 1. Sales for cash; 2. A policy designed to make the dealer a real merchant, actually performing the functions for which he is presumed to exist; 3. Bulk shipping from the factory, to the greatest extent

possible—shipments from branch warehouses to be discouraged; 4. Service no longer 'free'—to be paid for if and as delivered.

"Under this plan, our branch house organizations became substantially nothing but warehouse stations, with small stocks from which to make emergency shipments when dealers were unable to order a carload from the factory. Our sales force was greatly reduced; we now have forty-six men, no more than formerly might have served a single branch. We do not try to sell to every dealer; our aim is to get fewer and better dealers, making the territory of each one large enough so that he can develop a real volume of business. We have no more factory canvassers.

"Results are apparent in the reduction of expenses. We have done away entirely with costly credit and collection departments, and with many salesmen and branch house employees.

"Our rate of turnover has nearly doubled. We now turn our money about once in ten months, as compared with from eighteen months to two years formerly; and we foresee a time when we shall have two turns a year.

"We are securing a more satisfactory type of dealer; the man who has ready cash and the business acumen to use it for his advantage. We get, too, those desirable and energetic dealers who have bank credit. We miss entirely the risky fellows who have neither cash nor credit nor the energy to get them.

"Finally, there is the test of volume. Naturally, our volume suffered a terrific drop when we cut off all those extra lines. But I think I am safe in saying this: in the lines we retained, we have shown a greater increase in volume in the last year than anybody else in the industry. The plan and the company are no longer experiments. We have pushed our volume well into our area of profit. The company will make good money this year—more than it has made since 1918 and more, we believe, on a $3,000,000 capitalization than formerly with many times that capital.

"To sum up, I think we have learned unforgettably these truths: 1. It is a doubtful blessing to be able to offer customers, regardless of cost, a 'full line'; 2. A 'full line' is no blessing at all when a goodly number of the items have to be sold without profit or at a loss; 3. A huge volume of sales, by itself, is no measure of the success of a concern's marketing; 4. There may be very serious dangers in giving dealers too much assistance —they may become worthless to themselves and you; 5. When you are able to effect genuine economies in marketing, you will find a host of customers eager to share them.

"It cost us money to learn some of these things. We count the experience worth millions."

XI

HIGH PRESSURE DISTRIBUTION

It is possible to roughly classify a manufacturer as belonging either to those who "make" products to meet requirements of the market, or as belonging to those who "distribute" brands which they decide to make. The manufacturer in the first class relies upon the natural demand for his product to absorb his output. He relies upon competition among wholesalers and retailers in maintaining attractive stocks to absorb his production. The manufacturer in the second class creates a demand for his brand and forces wholesalers and retailers to buy and "stock" it. In order to market what he has decided to manufacture, he figuratively has to make water run uphill.

The business world tends to overlook the fact that even in this era of high pressure marketing, competition among buyers to secure what they need is still the greatest factor in the distribution of products. Most of the commodities we produce are bought not because producers desire to sell them, but because consumers desire to buy them. If both our price system and our distribution sys-

tem were absolutely perfect, producers and manufacturers could entirely rely upon the competition between wholesaler and wholesaler, and retailer and retailer for goods which they could resell to consumers advantageously, to absorb all that our industries are capable of producing.

Even under the abnormal conditions prevailing today, manufacturers whose factories are situated with regard to raw materials and labor conditions so as to produce economically, can rely upon brokers to hunt out their factories for the privilege of selling their products. Competition between brokers and selling agents for the right to sell the products of such manufacturers is keen. The broker's most valuable assets are his franchises entitling him to sell the products of factories which offer the market desirable products at reasonable prices.

The primary step toward profits in merchandising is intelligent buying—not skillful salesmanship. The primary requirement for success in wholesaling and retailing is that buying be at least as efficient as that of competing wholesalers and retailers.

The present day preoccupation with the idea that profits are to be made only by increasing sales volume, has tended to make business men overlook this fact. As a result, buyers today are not nearly so keen in their hunt for sources of supply as they were formerly. And manufacturers, who have found that the buyers were no

longer seeking them out so aggressively, have all the more readily been persuaded to turn to high pressure distribution in order to win markets for their production.

Yet it is still a fact, and will probably always be a fact, that the factory which sells only in its natural field because that is where it can serve best, meets little sales-resistance in marketing through the normal channels of distribution. The customers of such a factory are so "close" to the manufacturer, their relations are so intimate, that buying from that factory has the force of tradition. Such a factory can make shipments promptly; it can adjust its production to the peculiarities of its territory, and it can make adjustments with its customers more intelligently than factories which are situated at a great distance. High pressure methods of distribution do not seem tempting to such a factory. They do not tempt it for the very good reason that such a factory has no problem to which high pressure distribution offers a solution.

It is the factory which has decided to produce trade-marked, uniform, packaged, individualized, and nationally advertised products, and which has to establish itself in the national market by persuading distributors to pay a higher than normal price for its brand, which has had to turn to high pressure distribution. Such a factory has a selling problem of a very different nature from that of factories which are content to sell only where

and to whom they can sell most efficiently. The factory which determines to secure nation-wide distribution of its brand, and which must therefore conceal in some way the fact that it cannot sell its products with equal economy in all sections of the country, turns to high pressure distribution, because it does offer it a means for evading the consequence of its high cost of marketing.

The proponents of high pressure distribution, the advertising men and salesmanagers of the modern school, use the word "distribution" in a manner distinctive to themselves to describe the marketing problems of such manufacturers. A national advertiser, for instance, does not sell his brand in the ordinary sense of the term. He does not try to convince the trade of the merits of his product and of the reasonableness of the price which he asks for it. He subordinates discussion of the intrinsic value of his product to discussion of its resalability. Intrinsic value ceases to be the criterion by which his product is judged by wholesalers and retailers. It is replaced by the criterion of consumer demand. Thus the manufacturer does not have to "sell" his brand to wholesalers and retailers; all that he has to do is to "distribute" it; to "stock up" wholesalers and retailers with it so that consumers may be able to buy it.

"Distribution" to the national advertiser means the process of placing a brand in the hands of

wholesalers so that retailers may be enabled to buy it, and of then placing it in the hands of retailers so that consumers in every section in which he advertises may be enabled to buy it. In stocking-up retailers and wholesalers he is absolved from the necessity of convincing them that his brand is good value to the extent that he is able to convince them that the consumer demand for it will insure resalability and speedy turnover.

Distribution of this sort is absolutely essential to the existence of any manufacturer who refuses to rely upon the natural demand on the part of wholesalers and retailers for the product he manufactures, and who must resort to artificial stimulation of sales to insure a profitable volume of production. High pressure marketing thus creates "sales resistance"—an acute distribution problem which otherwise would not exist. It thrusts upon the manufacturer a double task: first, that of persuading the ultimate consumer to demand his brand, and secondly, that of overcoming the resistance of wholesalers and retailers to the addition of still another brand to the brands already being stocked by them. To such a manufacturer, wholesalers and retailers do not represent opportunities for the sale of goods; they do not function as markets for products; they are mere sales-resistances to the distribution or stocking up of his brands.

Two alternative methods of solving the problem of distribution are open to the manufacturer who

has to overcome wholesale or retail sales resistance because he is trying to create consumer demand for his brand. He may decide to force distribution through the regular outlets for his products by bending wholesalers and retailers to his necessities, or he may create new outlets and, so to speak, travel right around the sales-resistance of the regular outlets.

Manufacturers in some industries have successfully reduced wholesalers and retailers to slot machines which simply vend their products. They distribute through the regular outlets because the cost of creating alternative outlets would be greater than the value of the additional business they might be able to secure through them.

Other manufacturers have either established new outlets or created new channels of distribution for their products. They passed either right around the wholesalers in order to reach retailers direct, or around both wholesalers and retailers in order to reach ultimate consumers. If wholesalers presented too formidable a sales resistance to the distribution of their products, they formed wholesale departments of their own and sold their products direct to retailers. If the opposition of both wholesalers and retailers proved to be too formidable, then they sold direct to the public, some of them through retail stores of their own, others through the United States mail, and still others through house to house canvassers.

The steady rise in prices during the past fifty years and the resulting hue and cry about the exactions of the middleman have made it very easy for any manufacturer to justify these costly methods of "direct" distribution. The manufacturer who apparently eliminated middlemen was looked upon as a public benefactor. The popular hunger for buying "direct" from the factory and cutting out middlemen's profits has furnished a fertile soil, in which new channels of distribution and new wholesale and retail outlets, created to promote the manufacturer's own interest, have multiplied and flourished. High pressure stocking-up and high pressure distribution by these manufacturers has reduced distribution to a state of anarchy, in which each factor in distribution is a law unto himself, and in which the general well being of producers, distributors, and consumers is needlessly sacrificed.

XII

HIGH PRESSURE WHOLESALING

The independent wholesaler presents the first obstacle to the progress of the manufacturer engaged in high pressure marketing. Such manufacturers challenge the wholesaler's dominance of the channels of distribution. A whole technique of high pressure wholesaling has been devised by sales promotion managers and advertising men for the purpose of overcoming the sales resistance of these independent wholesalers.

The modern specialty salesman is one of the most interesting instruments of the technique developed to overcome wholesaler sales-resistance in those cases in which manufacturers sell through independent wholesalers.

In the distribution of groceries, the operations of specialty salesmen have reached a state almost of perfection—from the standpoint of the manufacturer. What the wholesale grocer thinks of the specialty salesman can be imagined from what one of them said in the course of an article [1] discussing this phase of present day marketing.

[1] John D. Houston of James W. Houston Company, Pittsburgh, Pa., wholesale grocers, in *Printers' Ink*, January 18, 1923.

The manufacturer's specialty salesman is the pirate of the grocery business. He has but a selfish interest in the retailer and looks with contempt on the jobber. He knows nothing of the financial standing of the retail merchant, cares nothing for the jobber's expense of doing business, overloads the weak retailer, cuts prices to the strong and then turns the orders over to the jobber with the remarkable guarantee that they are genuine.

One of the most successful manufacturers of a grocery specialty operates substantially as follows: A territory in which his product is to be introduced is selected and to it is dispatched a crew of specialty salesmen. The product which they are to induce the jobbers in that territory to purchase from the manufacturer is a baking powder. They do not, however, begin by calling on the wholesalers and trying to sell them a stock of their baking powder. Instead, they proceed as follows: First, the territory is divided among the members of the crew. Then each specialty salesman makes a canvass of consumers near one of the retailers they propose to "get" and who buys from one of the wholesalers they propose to stock-up. The consumer canvass is a door to door demonstration to the housewives of the merits of the baking powder. The demonstration may range all the way from a brief chemical test to the actual baking of a pan of biscuits. No matter how long and costly, the demonstrations continue until a sufficient number of orders have been secured from housewives. Orders on retailers is what the

salesman wants—so he sells the consumer nothing. As soon as the salesman has a sufficient number of such orders from the housewives to justify him in approaching the grocers assigned to him, he calls upon them and presents the baking powder orders to them.

Each retailer is now placed in an embarrassing predicament. He probably has none of the powder in stock. He may be amply supplied with the half dozen brands which his customers have been using satisfactorily for years. To add still another brand to his stock will result in dividing his present volume of baking powder sales among seven brands instead of six. He will be increasing his stock of baking powders without correspondingly increasing his total volume of sales.

The grocer, even though he may not analyze the situation so carefully, is yet instinctively averse to the addition of the new brand. With every new brand he runs the risk of adding a slow moving, perhaps even an unsalable item, to his stock. But the specialty salesman's orders put him to the difficulty of either refusing to fill orders from his customers, and thus incurring their displeasure, or of placing an order for the baking powder. Naturally the average grocer yields to the apparent demand of his customers and gives the salesman an order to be shipped to him through the wholesaler with whom he does business. Then by offering the retailer some special "deal," the salesman loads him up with the new

brand as heavily as he can, so as to force the dealer to push the new brand and to cut down on his purchase of the old brands.

When the entire crew operating in the district has in this way secured a sufficient number of orders on the wholesalers from the retailers, the manager of the crew calls upon the wholesalers one after another and places each of them in the same dilemma in which the retail grocers had been placed. The wholesalers may also be well supplied with all the baking powders for which there had been calls in their territory, but no matter how averse they may be to increasing the number of brands they stock, the fear of displeasing some of their retail customers constrains them to place an order for the new brand.

The baking powder has now been "distributed."

Either of two things follows: the brand "repeats," or it fails to "repeat." If the housewives fail to continue buying it, each grocer finds himself loaded down with a lot of dead stock. And each wholesaler finds himself loaded down with a much larger quantity of a brand of powder which is unsalable or salable only at a great loss. The losses which both wholesalers and retailers suffer in this way become a part of their total cost of doing business and are ultimately passed on to the consumer in the general mark-ups of wholesalers and retailers.

If, on the other hand, the new baking powder proves to be a "repeater," there is a diminution

of the sales of the old brands, but as we shall see, with the same net result: a stock of baking powder larger in proportion to sales than was carried previously by both wholesalers and retailers.

But the competitive baking powder manufacturers do not remain inactive while this manufacturer is introducing his baking powder. As soon as they hear of the drive of the new manufacturer, all the old manufacturers send their specialty salesmen into the territory. These men duplicate the operations of the first manufacturer's crew, go to the dealer with all kinds of "special deals," load him to the guards with their brands, and really force him to continue all the old brands, even though he has already on hand enough of the new to amply supply his trade.

Is it any wonder that the trail of the specialty salesman; that high pressure wholesaling by manufacturers who distribute through regular wholesalers, is marked by deals, rebates, dead stock, dissatisfied and injured merchants and wholesalers—as Mr. Houston says, by "commercial murder"?

Let us now consider high pressure wholesaling when the manufacturer decides to establish his own system of wholesaling.

SELLING DIRECT TO RETAILERS

In 1909 there was an epidemic of criticism of rising prices. The press, the pulpit, and the people reported, exhorted, and excoriated. Chronic criticisms crystallized into the phrase, "the high

cost of living.'' Consumers blamed retailers. Retailers placed the responsibility upon wholesalers. Wholesalers, aware of the fact that the manufacturer's cost of production had dropped, were unable to blame the manufacturers. Unnecessary ''middlemen'' were charged with the chief responsibility for the rise in prices. The ''middleman'' was supposed to be the wholesaler. There was widespread criticism of wholesalers.

Manufacturers in increasing numbers began to eliminate the wholesaler from their scheme of distribution and to sell retailers direct.

One of the leading wholesalers [2] of the country describes just what has resulted in the dry goods field from the efforts of manufacturers who sell retailers direct.

> The result was exactly what might have been expected. Where the manufacturer had used three or four salesmen, he had to increase the number to forty or fifty. Where his Credit Department had easily handled the comparatively few wholesale accounts of high grade credit, he had to add scores more people to handle the increased detail of more doubtful accounts. Where his Shipping Department had handled case and carload shipments with very little effort, it now became necessary to handle thousands of parcel post, express, and freight shipments with the resulting increased expense.

[2] Willis P. Munger, of the Burnham-Munger-Root Dry Goods Company of Kansas City, Mo., in an article entitled, ''The Wholesaler, the Hub of Service,'' written for *The Midwest Merchant*.

The manufacturer's line restricted to the articles he made himself, embraced a very small part of the retailers' requirements, reducing the amount of the individual sales and raising the cost. To overcome this, he fixed minimum quantities at a point disastrous to his new customers, slowing up their turn-over and reducing their discounts. Very soon his salesmen were complaining about slow deliveries and advocating warehouses situated at points in the country that would result in speeding up the service demanded by the retailer; in a great many instances this was done, enormously increasing expense. Then bankers, loaning money to manufacturers, began to ask pointed questions about increased cost, and were told that the wholesalers were back numbers, and that the up-to-date method was to distribute direct. They confided to their bankers all the terrible things the "middleman" was doing, and had done; but the banker could not get the increased cost in clerk hire, salesmen, shipping, and credit expense out of his mind.

A little later the retailer began to get restless and to realize that something was wrong. His statement, "I buy direct," was losing its ring of enthusiasm and he started to analyze his difficulties. He found that most of his time was occupied in looking over great numbers of short lines; his selections did not seem to work out right; women had suddenly developed erratic ideas about qualities and styles, and he was using P.M.'s and special sales to keep his stock moving. Adjustments on short shipments, damaged goods, back orders, and substitution seemed to be more difficult, and more annoying than they had been in the past, and almost impossible to bring to a final settlement. Every manufacturer was

insisting upon advertising coöperation on the newly installed brands, special "so and so" days, premiums offered to his sales force, window displays, the word "pep" seemed to come at him from every direction, and was getting on his nerves.

THE SURVIVAL OF THE INDEPENDENT WHOLESALER

To anyone who has observed the steady effort in the past decade to eliminate the wholesaler as a factor in distribution, it is disconcerting to discover after all these years, that the wholesaler is still the hub of our distribution wheel.

It is still necessary for the economical distribution of merchandise that manufacturers be enabled to ship in quantity. The wholesaler is essential if the economy of carload or quantity shipping and selling from the factory is to be maintained.

It is still necessary to have a reservoir of supply in each of the important distributing centers of the country, so that retailers will be enabled to draw upon the reserve at a moment's notice and not have to wait for shipments from the distant manufacturing centers. The wholesaler is essential if these reservoirs of supply are to be provided most economically.

It is still necessary that somebody break bulk and redistribute stock from the various shipping centers of the country and the wholesaler is still essential if this service is to be most economically rendered to the community.

It is true that independent wholesalers today do not control the channels of distribution as fully as was the case fifty years ago. If the existence of alternative methods of distribution be an advantage, then the existing maze of distributing channels represents progress.

Fifty years ago merchandise moved from manufacturer to wholesaler to retailer to consumer almost exclusively.

Today, some of it moves from the factory direct to the consumer.

Some of it moves from the factory to the manufacturer's store and then to the consumer.

Some of it moves from the factory to the independent retailer or to the mail order house, department store, or chain store, and then to the consumer.

Some of it moves from the factory to the manufacturer's district warehouse, then to the manufacturer's retail store, and then to the consumer.

Some of it moves from the factory to the manufacturer's district warehouse and then to an independent retailer and then to the consumer.

Some of it still moves from the factory to the independent wholesaler to the independent retailer and then to the consumer. More of it moves in this way than most people realize. In spite of the retailer's hunger to buy direct, and the desire of manufacturers to eliminate him, the wholesaler still moves the bulk of the goods sold at retail. If the proponents of the theory that he is unneces-

sary to economical distribution are correct, here indeed is an enigma. How does so inefficient an instrument survive? What is the secret which enables this middleman to survive the competition of the actual producer who sells direct?

The system of wholesale distribution through independent wholesalers survives because it serves more economically than does any other system.

The independent wholesaler may be an unnecessary middleman to the retailer—especially the large retailer. He may present formidable sales resistance to the distribution of the products of the over-ambitious manufacturer. But he can point to the fact that it is hardly progress to have increased the number of channels of distribution and to have also increased the total cost of distributing our products. For that is what high pressure wholesaling frequently does—it creates additional channels of distribution generally more costly than the old. It makes each manufacturer duplicate the wholesaler's activities; it produces duplicate selling staffs; duplicate credit departments; duplicate accounting departments; duplicate shipping departments. It reduces the relative volume of business transacted through the regular wholesaler without reducing prices to the consumer. It benefits only those manufacturers fortunate enough to succeed in creating consumer demand and "putting it over" on wholesalers, retailers, and consumers.

XIII

HIGH PRESSURE RETAILING

It is retailing which is, according to the advocates of high pressure distribution, the real neck to the distribution bottle. Manufacturers anxious to force their products into distribution find this neck so choked up that it is impossible for them to secure retail outlets in every community in which they wish to place their products on sale. The fact that the choking up of the neck of the bottle might indicate that the retailers were already amply stocked with merchandise, or that generally they were so overstocked that additional lines would simply increase their stock of goods without a corresponding increase in volume of business is, of course, an explanation of the retailers' resistance to the addition of the manufacturers' lines, but it is no solution of the dilemma in which the manufacturer seeking high pressure distribution finds himself.

How are these manufacturers trying to escape from this dilemma?

Exactly as in the case of the sales resistance presented by independent wholesaling—either by re-making the retailer into a mere slot-machine,

or by abandoning distribution through the regular retailer altogether.

In certain lines of retailing—groceries and drugs are the most conspicuous—the manufacturers have pretty well succeeded in making the old time food merchants and the old time pharmacists into slot machines that vend indiscriminately the products which they are persuaded to distribute.

In other lines, they have abandoned distribution through retail stores altogether to sell direct by mail, through canvassers, or through chains of retail stores of their own.

The country is dotted with innumerable warehouses—established by manufacturers so as to eliminate or to coerce independent wholesalers—and by an even greater number of manufacturers' retail stores established to give manufacturers retail outlets where otherwise they would have none.

Stores of his own enable such a manufacturer to get "his" share of each community's business. The business in his product is then divided between the stores already in existence and the stores established by the manufacturer. There is, of course, no substantial increase in the volume of merchandise moved into each community, and the fact that it has to carry the cost of maintaining an additional store is a matter of indifference to the manufacturer if only he is able to get "his"

share of the total consumption of his product in the community.

It is possible to clothe the opening of retail stores and wholesale branches by manufacturers with an atmosphere of academic repute and scientific efficiency by calling it the integration of industry. The facts of the matter, however, are not altered by the change in nomenclature. The manufacturer simply takes on himself the performance of additional parts of the process of distribution. Only in exceptional cases can he perform it as economically as it can be performed by the independent wholesaler and retailer. Nevertheless he justifies it to himself fully and sufficiently if it enables him to meet the imperious necessity of distributing the volume of goods which he must sell in order to operate profitably.

An article in *Printers' Ink*,[1] discussing this subject, enumerates eleven advantages and six disadvantages in connection with the opening of retail stores by manufacturers. The advantages are the following:

1. The manufacturers' stores coöperate 100 per cent in backing up his national advertising.
2. Retail prices can sometimes be lowered.
3. Special service and adjustments can be rendered to customers more easily.
4. Substitution of other manufacturers' brands for his own is entirely avoided.
5. The consumers' taste can be studied at first hand.

[1] S. C. Lambert, *Printers' Ink*, February 3, 1921.

6. The product itself can be frequently improved as a result of direct contact with the user.

7. New and strong sales arguments can be developed.

8. A knowledge of retail costs and management is obtained which can be turned to account in dealing with independent retailers.

9. Advertising and display material can be studied and improved.

10. Commercial travelers can be trained in these stores.

11. Independent dealers can be persuaded to handle the line through the force of example.

This is a formidable list of advantages. To it must be added one which the writer of the article omitted. That reason is to secure an outlet for the manufacturer's line in a community where it is not possible to interest any existing retailer, or, in other words, to force his line of goods into the town.

The six disadvantages mentioned are in startling contrast to the glowing picture of service to the consumer and profit to the manufacturer, which a reading of the advantages seems to indicate. The disadvantages are:

1. Most of the stores have been operated at an actual financial loss. In nearly every instance it has taken years to get them on a paying basis.

2. There is great danger in trying to compete with the manufacturer's own retailers. If the manufacturer aims to sell his entire output through his own stores, this disadvantage does not exist. However, in most

cases the manufacturer who opens retail stores does so primarily as a lever for action upon independent retailers and when he tries to carry water on both shoulders, he often spills either one bucket or the other before he gets very far.

3. When independent retailers do handle the line, despite the competition of the manufacturer's stores, they do so grudgingly. They "back shelve" it and "knock" it at every opportunity. As a result, while the manufacturer's own stores may be successful, the antagonism of the independent retailers is so great that the distribution through outside channels is of very little benefit to the manufacturer.

4. A manufacturer operating his own stores is obliged to maintain very high standards. The stores must be operated on what might be called a luxurious scale in order to make a sufficient impression upon independent retailers. The overhead is so high that this is one of the reasons why these stores are so often financially unprofitable.

5. As is the case with all chain stores, it is important to have a high class store manager and these are very difficult to secure unless they are given more than a salaried interest in the enterprise.

6. The manufacturer's store is of necessity so occupied in trying to sell its own goods that it does not often respond quickly enough to popular demand. Consequently the independent retailer who has a more varied line is often at an advantage in competing with the manufacturer's chain store.

No statement which I might make of the philosophy underlying this form of high pressure

marketing would be half as vivid as some extracts from an address by R. T. Devlin, of the agency of Charles H. Fuller Company, Chicago, made to the Engineering Association.[2] While the illustration used by Mr. Devlin dealt with industrial marketing, in deference to the fact that he was addressing a gathering of engineering advertisers, what he said is equally descriptive of methods used in creating outlets for merchandise sold in retail stores.

Crashing the Gate. We have considered our problem in selling . . . the buyer already in business, but how about broadening the market? In order to illustrate how, with the use of general publicity, an indirect selling plan can be worked out to meet almost any problem we may have to face, I shall use as my example, a line of business where the manufacturers using our product are all assembled in one town. Here we have five manufacturers who can use our machinery and equipment. The manufacturers have not all the same buying power and one is more desirable than the others, because of the volume of business he does. It so happens that in this community we do not sell a single firm of the five. The town already has its quota of manufacturers. In fact, the last one is barely existing. Our salesman makes this town every other trip—it seems hopeless, and he is concentrating his time in productive territory.

We need a customer. We don't want No. 5—he's too small. No. 4 may not be any too prompt about paying bills. Our . . . advertising has just appeared once or

[2] *National Advertising*, January, 1925.

twice. Our man calls on Numbers 1, 2, and 3, and in each case he is met with comments on the advertising. It gets a rise, and our man is instructed what to do to take advantage of these comments. To make the problem more difficult, these firms do not change because of our . . . advertising. We have given them plenty of opportunity—now to get that customer.

Making a Customer. Our salesman goes to the Chamber of Commerce or the local bank—usually there are men who have saved some money and are anxious to go into business for themselves. The Chamber of Commerce and bank know of these men. As a result of our . . . advertising, they also know of our company and think they know all about the product we make. We are a recognized leader in our industry. A conference takes place with the men with the money. These men must also possess some intellect, in addition to the money. Our plan is laid before them—every step—the possibility of the market has been analyzed by us and the opportunity is there. These men accept.

Careful guidance on our part and in this market, which was already crowded, we have, in a few years, a picture slightly different from the first and very favorable to us because our new firm has taken its place as second in the community, and where we had no business before, we now have the second-best account in the city and with well-defined effort should have the leader with us because such a service cannot be ignored.

What a picture of the ruthlessness with which manufacturers operate—partly because they are tempted to exploit the ignorance of the business community generally, and partly because condi-

tions drive them to create new outlets or die. Just because a manufacturer insists upon an outlet in the community, a new firm is added to a field already so crowded by the existing five firms that two can barely subsist. The business of the community has to be thereafter divided among six firms instead of five, or the community must suffer the losses involved in the liquidation or failure of some of the original firms.

HIGH PRESSURE RETAILING THROUGH CANVASSERS

In a pioneer country in which stores are few and trading centers far between, the peddler and canvasser may perform a truly economic function in distribution. High as may be the cost of distributing goods through him, he has to be used because no other method less costly than that which he represents can exist. But in a densely populated and well organized country, house to house retailing represents, except in the case of very unusual products, the diversion of distribution from less costly distribution channels to more costly ones.

An amazing number of products are now being sold through canvassers. In addition to such things as books and sewing machines, which have been sold through canvassers from the very beginning, they include commodities so various as aluminum ware, coffee and tea, women's silk hosiery, lingerie, gas fixtures, electrical appli-

ances, raincoats, men's clothing, brooms and brushes.

An equally amazing number of men and women are employed in this particular form of high pressure retailing. Each manufacturer who distributes through house to house selling employs an army of these canvassers.

The activities of these armies of canvassers constitute a nation-wide duplication of the work of the regular wholesale and retail channels for distributing merchandise. Hundreds of manufacturers, some of them on a gigantic scale, are marshalling these armies and creating these duplications and reduplications of our channels of distribution.

The Fuller Brush Company, which makes a line of house brushes—a class of merchandise sold in practically every grocery, hardware, furniture, and general store in the country—employs over 2,000 canvassers, each one assigned to a territory containing a population of approximately 15,000, whose work is directed from over one hundred branch offices.

But the story of the Real Silk Hosiery Mills is even more interesting. More stores and more kinds of stores are engaged in distributing hosiery than any other product which men and women wear. It is sold in hundreds of thousands of stores—general stores, men's clothing stores, women's apparel stores, dry goods stores, department stores, haberdasheries, shoe stores, and

hosiery stores. No other article of apparel is quite so accessible to the consumer, and few articles of any kind sold at retail are the subject of keener competition in assortment, quality, and price. Yet in spite of all these facts, the Real Silk Hosiery Mills, of Indianapolis, Indiana, who claim that they have risen "in less than five years to undisputed world leadership in the manufacture of silk hosiery,"[3] and who sell exclusively through house to house canvassers, employ 10,000 canvassers operating from 250 branch offices for the purpose of making "Real Silk Hosiery Service almost indispensable to the efficient conduct of the American Home."

The support of these canvassers and the expenses of the men who recruit and direct them represent in very large part an entirely unnecessary addition to the cost of distribution. Every item of merchandise they distribute through their canvassers could be distributed through the ordinary channels of distribution with hardly any additional burden of overhead upon regular wholesaling and retailing. On the contrary, it would lower the cost of distributing all merchandise by spreading the existing overhead on a greater aggregate volume of sales.

An immense army of workers is thus diverted by this form of high pressure selling from more useful service in production, or in professional, public, or other service.

[3] *Saturday Evening Post,* January 16, 1926, pp. 48-49.

The President of the Fuller Brush Company, which did a business of 18 million dollars in brooms and brushes in the year 1924, and which has been growing at the rate of over three million dollars per year, all of their products sold through house to house canvassing, admits that his cost of distribution is not as low as the cost of selling through retailers.[4] In effect, he admits that as a result of his life work, every year over 18 million dollars worth of brooms and brushes, which in the normal course of events would have been distributed less expensively through retail and wholesale channels, are now distributed more expensively through the medium of house to house canvassing.

The possible growth of house to house retailing is limited only by the difficulty of securing and holding salesmen. The margin for profit is so large that the manufacturers employing it can indulge in all kinds of extravagances in order to speed up their business. Fortunately they cannot manufacture canvassers to order. No matter how effective their recruiting may be, even the most successful canvassing organizations lose their salesmen so rapidly that the total number of canvassers in the country increases rather slowly from year to year.

Mr. Bruce Barton, the author, editor, and advertising man, was at one time the manager of an extensive force of men engaged in selling books

[4] *Printers' Ink,* November 29, 1923.

from house to house. In an article describing his work he said: "I used to figure that two men out of a hundred were worth spending time on; but the percentage of men who actually stayed in our business and became permanent factors in it was far smaller than that. The process of sifting is fearfully expensive; the final salesman who is left represents a considerable investment in newspaper advertising and expensive drill. And once drilled, he may on the following morning desert to the opposition, or sink into the quicksands of life insurance or patent window shades. Men fail for various reasons—lack of courage, lack of endurance, dishonesty, drink—all these play their part, of course, and a sales manager must combat them as best he can. Thousands of men are advertised for every day in the city newspapers, given a quick canvass and turned out on the streets to fail, who might be saved if they were properly prepared. There grows up in our cities, therefore, a shifting, spineless company of professional applicants, their self-reliance and capacity utterly destroyed by repeated failures." [5]

According to Mr. Barton, one of the best small canvassing forces ever gathered together consisted of thirty-five men, and these were the final fit survivors of no less than five thousand applicants.

If only thirty-five men out of five thousand

[5] *Printers' Ink*, February 4, 1915, p. 3.

finally succeeded, it must be that 4965 men tried and failed. While it may be true that not all of these 4965 men worked for so long a time as to permanently injure their working morale, there can be no question about the fact that very few of them were benefited by their failure to make good.

The commission, salaries, bonuses, and prizes paid to canvassers make this method of selling expensive enough, but to this must be added the tremendous cost of recruiting such a force, keeping it at work, and replacing those who drop out of the ranks. Since it is not unusual to have an annual turnover of five hundred per cent. in a canvassing force, the arduous nature of the task before the sales managers of manufacturers who retail their product in this manner can be imagined.

One claim put forth by manufacturers who market their products in this expensive way deserves special consideration. Many manufacturers of specialties claim that unless consumers were persuaded to buy through house to house canvassing, there would be no market at all for their products. An executive of a concern selling vacuum cleaners said when asked about the costliness of introducing their product through canvassers, "Yes, this costs money. These men are able sales people and must be paid accordingly. Our cleaner sells for less than $75. If it were not for this system of selling, enabling us to obtain our present huge volume, our selling price would be $200."[6]

[6] *Printers' Ink.*

But as a matter of fact is a price of $200 really the alternative to a price of $75? According to this official, with a smaller production it would cost $125 more to manufacture the cleaner.

Large scale production, presumably, is made possible by the high pressure marketing thus reducing cost of production $125 on each cleaner.

As a matter of fact, really large scale production is made impossible by the high prices which have to be charged to cover the cost of high pressure marketing.

The principal reason that suction sweepers and similar appliances are high in price—and $75 is a high price—is because of the costly methods used in marketing them. The actual cost of fabricating them is only a fractional part of $75. But vacuum sweepers belong to that class of merchandise which lends itself to extremely high powered selling. So long as manufacturers believe that greater profits are to be made by adding to the cost of distribution rather than by securing volume through economical marketing, those using this costly method of retailing will try to put a flavor of public service into their methods by claiming that their products would cost much more if they sold them through regular wholesalers and retailers.

Most products which are sold by a campaign of house to house canvassing, installment credit and national advertising, as is the case with the vacuum cleaners, represent a factory cost of only

from one-fifth to one-tenth of the price paid for them by the ultimate consumer. All the rest represents various kinds of distribution costs. If vacuum cleaners were to be sold through the normal channels of distribution with a normal advance over their manufacturing costs, an enormously greater market for them would develop. As it is, the very fact that consumers are asked to pay from five to ten times the manufacturing cost creates tremendous resistance to their sale.

Consumers who believe that the manufacturer who sells through house to house canvassers undersells the local retailer, base that belief upon the cleverness of the national advertising of manufacturers using this method of distribution and upon the silvery sales talk of their canvassers. The average consumer who buys from canvassers does have a vague feeling that by buying "direct" he is saving money. But in the very nature of the case, the manufacturer who sells direct cannot actually undersell the average retailer. It costs far too much to operate his complicated organization. With such a costly method of retailing, it is only natural that most of the products sold by canvassers cost the consumer more than he would pay for them to his local dealer.

There remains for final consideration only that justification made for house to house retailing which is symbolized by the word "service." But does the house to house canvasser better serve the consumer than does the local retailer? Cer-

tainly the retail store with its stock of merchandise within reasonable distance of the consumer thus making it possible for the consumer to promptly secure the merchandise which he may want whenever he desires to buy it, serves the average man or woman much better than does any other method of retailing. Not only does it render superior service in most cases, but it also renders it at a lower cost. But unfortunately for retailers—both retailers and retail sales clerks usually lack the eloquence of the proponents of canvassing and so have less success in presenting the merits of their service.

Costly methods of retailing survive principally because the relative cost of distribution through the regular channels of wholesaler-retailer-consumer and through the various so-called "direct" channels have not been investigated. Such investigations would very quickly establish, not the perfection, but certainly the overwhelming superiority in efficiency and economy of over-the-counter retailing.

XIV

HIGH PRESSURE SELLING

The census of 1870 lists 7,262 commercial travelers.

The census of 1920 lists 179,320.

In 1870 commercial travelers were .06 per cent. of the total number of persons ten years of age and over employed in gainful occupation.

In 1920 they were .43 per cent. of the total number of persons employed.

The percentage of the population classified as traveling salesmen increased 716 per cent. in the period of fifty years, while the actual number engaged in this branch of distribution increased 2,469 per cent.

The transformation in methods of salesmanship is as startling as the increase in numbers of those engaged in selling. Modern methods of salesmanship and of sales-management represent an almost complete abandonment of rule of thumb methods. The happy-go-lucky salesmanship of the pre-McKinley era has been replaced by methods based upon scientific analysis of the psychology of the prospective buyer. The scientific methods of today have, however, failed to reduce the

numbers of salesmen necessary to the accomplishment of the task of selling. In production, the development of more efficient processes is followed by a reduction in the numbers of laborers necessary to the performance of a given task. In distribution, efficiency engineers and scientific management are apparently being flouted. The science of salesmanship becomes more and more scientific each year, and yet more and more salesmen are necessary in order to dispose of the products of our factories.

Prior to the Civil War, the traveling salesman was practically non-existent. The traders of the pre-railroad period visited the markets in person, for one reason because it was often necessary for the merchant to freight the merchandise back by wagon under his own direction.

The prototype of the modern salesman was the "greeter" of the early saloon era. These greeters were employed by the wholesalers to greet and entertain visiting merchants. Manufacturers employed few salesmen because their products were disposed of to the wholesalers, generally through independent brokers, and the demand for factory products was on the whole sufficient to make intensive selling by them unnecessary.

As the manufacturers emerged more and more as the dominant factors in distribution, the number of salesmen employed by them increased. The movement to eliminate the wholesaler and to subordinate the wholesaler and retailer to a system of

national distribution required the use of large numbers of specialty salesmen by the manufacturers. With their appearance on the scene, the numbers of traveling salesmen increased with amazing rapidity.

The late Arthur E. Sheldon was the founder of the school of high pressure salesmanship which dominates methods of selling today. A keen student of psychology, Sheldon discovered than an understanding of certain facts in psychology would be of great assistance to the salesman having to persuade reluctant buyers to buy.

Prior to the formulation of the principles of salesmanship by Sheldon, salesmen were the products of an apprenticeship lasting years, which familiarized the prospective knight of the road with the nature of the product, the sources of the raw materials, the methods of manufacture, and standards of quality and value.

The embryonic salesman started his career by taking care of stock in the wholesale house which he sought to represent. He continued in this capacity until years of actual handling of the merchandise had thoroughly familiarized him with grades, kinds, stocks, and methods of ordering, shipping, accounting, and credit. A pleasant personality was of course an asset to the salesman, but the ability to hypnotize the prospect was not permitted to obscure the need of familiarity with the product which the salesman was to sell.

The salesman of today is under no such neces-

sity to master some line of merchandise. He is a master not of merchandise, but of psychology. The text books on modern salesmanship and the courses in scientific salesmanship are not courses in which merchandise is studied. They are courses in applied psychology.

If it were to be generally accepted that individuals buy because they want goods, and consult catalogues and salesmen merely for the purpose of ascertaining the price, the very foundations of modern salesmanship would be overthrown.

There is, of course, a real need for the salesman. The buyer must somehow or other secure information concerning the merchandise for which he is in the market. If there were an even equation between the demands of the market and the offerings of the producers, the work of the salesman would be reduced to that normal basis of furnishing information which is at present merely a beautiful ideal. Unfortunately, the pressure upon the producer to sell is so much greater than the capacity of the consumer to buy that high pressure methods of selling have invaded pretty nearly every industry.

The result is that buyers suffer from a veritable plague of salesmen. They can escape from them only by arbitrarily limiting the days of the week or the hours in the day when they will see salesmen. Salesmen travel hundreds of miles, stop at expensive hotels, principally in order that they may cool their heels the greater part of their

days waiting for buyers to see them. Is it any wonder that this method of selling—normal and natural in most cases—costs much more than it should?

An interesting analysis of the cost of selling is made by William R. Basset, President of Miller, Franklin, Basset & Company, accountants, in an article discussing this subject from the standpoint of the manufacturer.[1] There are three reasons according to Mr. Basset for uneconomic use of salesmen:

Pride, advertising in periodicals of national circulation, which, unless much of the circulation that is paid for is to be wasted, must be accompanied by national distribution, and the general lack of knowledge as to what it costs to sell.

Take the small business which is selling say $300,000 a year in a small territory in the vicinity of the plant. Its total cost of selling is $24,000 a year, which gives, as commonly figured, a selling expense of 8 per cent. If this figure has been maintained for three or four years most people assume that some occult power has ordained that 8 per cent shall now and forever be the selling expense for that business provided some nefarious outside influence like cut-throat competition does not knock it into a cocked hat.

It follows, according to that line of reasoning, that $1,000,000 worth of business can be secured at a selling cost not greater than $80,000, and $10,000,000 worth (which is what national distribution would mean) for

[1] *Advertising and Selling Fortnightly.*

$800,000. In fact, since the factory increased volume often brings a lower rate of overhead, it is usually expected that with national distribution the percentage cost of selling will go down. Perhaps it would drop to 7 per cent or even to 6 per cent—who knows?

Yet it may cost nothing to sell an old customer who sends his $100 order through the mail, and it may cost $500 to open a new account with an order of the same size.

In some parts of the country a salesman for this company could make only one call a day at a cost ranging from $80 to $130 per call.

Usually the direct cost of the salesman—his salary and expenses—is much the smallest part of the total.

It is not possible in a short article to describe in detail all of the calculations that must be made to determine the cost per call for even one business. It will be apparent, however, that each man must bear a fair share of the general sales expense.

He must be supervised. There is expense in the general and branch sales offices for clerks, stenographers, rent and supplies. The officers of the company, such as the president, give some of their time to sales problems, so the salesmen must bear part of that cost.

Presumably the advertising makes his way easier, so he should be charged with some part of it, the amount to be determined in ways which will hardly be the same for any two concerns. Sometimes it may be right to charge him with a share of the general advertising. Certainly any direct advertising sent to the people he sells will be borne by him. And usually any advertising which he furnishes to his retailers should enter into the cost per call.

When all of these proper items of selling expense are figured in it is not hard to see why the cost per call often runs over $100 as it did for the manufacturer whose problems I am describing.

The owners of this concern were convinced that all wholesalers were about as useful to the economic system as is a tape-worm to the human body. Consequently they went direct to the retailer in all territories.

When the sales in the territories west of Denver were charged with the actual cost of selling on the cost per call basis instead of with the per cent selling cost for the company as a whole, it became evident that fully a third of the net profit made in the East was being lost in the West.

As a result the company approached several strategically located jobbers in the West who, between them, could effectively cover the territory. These jobbers were willing to handle the line on a margin which left the manufacturer an entirely satisfactory profit. Because the jobbers' salesmen were already traveling the territory with other lines the jobbers could make a profit. Everybody was happy.

It appeared in cold figures that an order of any size from an old account was far more profitable than one from a new dealer. Yet this company spent, in round figures, a quarter of a million dollars a year merely to replace the dealers who had left the fold. Many of them strayed because they felt they were not getting the attention they should get and believed that other manufacturers would value their orders more highly.

Out of the abundance of his experience, Mr. Basset comes to the conclusion that the mania for

volume of sales results in less profit to manufacturers. As Mr. Basset puts it, "There is hardly a large business that has come under my observation but what could make more money by doing less business."

To the philosophic turn of mind, there is something excruciatingly funny in this demonstration of the fact that high pressure salesmanship is not only unjustified from the standpoint of the consumer, but that it is unjustified from the standpoint of the manufacturer himself.

XV

HIGH PRESSURE ADVERTISING

There may be too much advertising today. There may be too much advertising by retailers, too much advertising by bankers, too much advertising by manufacturers. Anyone, however, can say that there is too much merely because it is large in quantity. We have unfortunately no standard by which to determine the amount of advertising which might be done usefully and in excess of which advertising represents waste. It is idle therefore to merely rail against volume of advertising. It is necessary for us to study the objectives of the various kinds of advertising in order to determine whether advertising in whole or in part serves a useful purpose.

Now, the economic consequence of national advertising, of what is here called high pressure advertising, differs from the economic consequences of retail advertising, of financial advertising, of industrial and of trade advertising.

High pressure advertising does not answer to the definition of advertising to be found in the dictionary: "To inform or apprise; to make known through the press."

The immediate objective of national advertising is to secure brand specification—to create consumer demand or consumer acceptance of the advertisers' brand. The definition of national advertising should be: to create brand specification by consumers through the medium of printed statements.

That advertising served a useful purpose when a merchant printed the fact that he was in receipt of a shipment of New Orleans molasses or of Scotch ginghams, no one can possibly question. This was information of value to the public a hundred years ago and similar information is of value to the public today. Advertisements which describe the goods which a retailer has on sale and the prices at which he is selling perform a useful service. The retailer's advertisements, it is true, are probably not performing that service at maximum efficiency, and he may for that reason spend more for advertising than is really necessary. But if he makes that mistake, he pays for it, since competition with other stores prevents him from raising prices on his merchandise to cover his inefficient advertising.

The situation as to the national advertising of manufacturers is very different.

The purpose for which the manufacturer advertises is not primarily to "inform or apprise."

"Such a conception of advertising is now not only inadequate, but false and misleading," says

George French.[1] "It is now one of the minor functions of advertising to announce or give notice. Its major function is to persuade."

Selling merchandise to the consumer by the use of national advertising is selling merchandise in a very different way from that which prevailed in less strenuous times. Then merchants used to assemble goods and await the demands of the public. Both the makers and the storekeepers supplied the necessities of the public, but permitted the public itself to develop its own needs and propensities to purchase. Customers went to the stores because necessities, rather than artificially created desires, had developed in their lives. They bought goods when their pantry shelves were emptied or their clothes were worn out. The new things they bought were needed principally to replace those which had been consumed.

The end sought through national advertising is the reverse of that which the dictionary describes and that which still forms the theme of most of the advertising of merchants today. The object of national advertising is to create desire. It ignores the question of the necessity for the goods and tries only to succeed in persuading the public to buy what the advertiser offers. At the best, the needs of the people form but one of the smaller considerations in the plans of the manufacturer who advertises. He bends his energies to the

[1] "Advertising," George French.

task of persuading people to buy his trademarked goods, and he has no occasion to concern himself about their utility in economic life. He often not only manufactures the goods, but through his advertising, manufactures the demand for them. He creates, as George French says, a necessity in the lives of the people that has no economic or moral basis in fact.

Surely, if one of the ablest thinkers upon the subject of advertising characterizes consumer demand created by national advertising as having "no economic or moral basis in fact," we may term the business created by a manufacturer in this way as artificial demand.

GROWTH OF NATIONAL ADVERTISING

During the year 1925 the probable expenditures of national advertisers for creating this artificial demand was around $1,000,000,000.

Year by year the expenditure has been increasing.

It is difficult to estimate accurately the rate of increase, but if we assume it to be substantially the same as the rate of increase of the advertising inserted in leading magazines of the country, we shall probably come very near the actual rate.

In 1915, advertisers spent $38,737,336 in 76 monthly and weekly magazines, women's publications, and farm journals. In 1916, they spent $51,867,803 in 77 publications; in 1917, in the same number of publications, $57,793,628; in 1918, in 72

publications, $61,312,888; in 1919, it was $97,208,-791; in 1920, it was $132,414,799.

This would indicate that the expenditure was more than trebling itself every five years. As, however, the year 1921 (the year of deflation), showed a reduction in advertising in these publications to $95,439,236, this rate would be too high.

A very conservative estimate based upon these figures would be that the expenditure more than doubles itself every five years.

This means that if the expenditure for national advertising was $1,000,000,000 in the year 1925, it will be $2,000,000,000 in 1930; $4,000,000,000 in 1935; $8,000,000,000 in 1940, and so on ad infinitum to the advertising millennium.

Even those who have carefully observed the growth of national advertising and who have noted from year to year the growth of the circulations of the national mediums, the increases in the amount of advertising in them, and the sizes of spaces used by individual advertisers, find it difficult to visualize the magnitude of the industry which may ultimately be devoted to national advertising. It is already an industry that has attracted thousands of the ablest minds of the country, and diverted from other more productive industries great armies of workers in paper making, printing, engraving and allied fields. The raw materials used in the industry, the pulp wood, coal, lead, copper, zinc, represent great drafts upon the natural resources of the earth.

By combining the figures issued by the Crowell Publishing Company, of New York, giving the expenditures of leading national advertisers in thirty magazines with the estimated volume of advertising by national advertisers in newspapers prepared by the Bureau of Advertising of the American Newspaper Publishers Association, we get the following table:

1924 EXPENDITURES (IN NEWSPAPERS AND MAGAZINES ONLY) BY LEADING NATIONAL ADVERTISERS

	In Newspapers (*See Note 1*)	In Magazines (*See Note 2*)	Total
1. Victor Talking Machine Co.	$ 1,900,000	$ 1,184,310	$ 3,084,310
2. Ford Motor Company	2,000,000	651,250	2,651,250
† 3. Chevrolet Motor Car Company	1,650,000	552,065	2,202,065
* 4. Postum Cereal Company	875,000	1,274,830	2,149,830
* 5. Procter & Gamble Company	510,000	1,409,050	1,919,050
6. American Tobacco Company	1,600,000	298,691	1,898,691
7. Dodge Brothers	1,200,000	641,600	1,841,600
8. Colgate & Company	450,000	1,158,455	1,608,455
9. Congoleum Company	400,000	1,181,900	1,581,900
* 10. Campbell Soup Company	.....	1,519,200	1,519,200
11. Liggett & Myers Tobacco Co.	1,500,000	.....	1,500,000
12. Standard Oil Co. of Indiana	1,500,000	.....	1,500,000
13. Calumet Baking Powder Co.	1,400,000	.....	1,400,000
14. Pepsodent Company	800,000	561,303	1,361,303
15. Willys-Overland Co.	500,000	859,850	1,359,850
16. Lever Brothers Company	.....	1,339,350	1,339,350
* 17. Wm. Wrigley, Jr., Company	1,250,000	.....	1,250,000
18. Corn Products Refining Co.	800,000	384,300	1,184,300
19. H. J. Heinz Company	600,000	527,970	1,127,970
20. Palmolive Company	300,000	785,270	1,085,270
21. Buick Motor Company	635,000	435,500	1,070,500
22. United States Rubber Company	750,000	309,410	1,059,410
* 23. Hupp Motor Corporation	750,000	295,980	1,045,980
24. Paige-Detroit Motor Car Co.	1,000,000	.....	1,000,000
25. Sun-Maid Raisin Growers Assn.	465,000	518,050	983,050
26. Quaker Oats Company	400,000	532,580	932,580
27. Andrew Jergens Company	150,000	777,875	927,875
28. Lambert Pharmacal Company	150,000	769,039	919,039
* 29. Borden Sales Company, Inc.	380,000	503,000	883,000
* 30. Vacuum Oil Company	125,000	752,000	877,000
* 31. Armstrong Cork Company	400,000	423,700	823,700
32. Eastman Kodak Company	250,000	566,845	816,845
33. Hart Schaffner & Marx	500,000	284,775	784,775
34. Swift & Company	.....	763,960	763,960
35. Metropolitan Life Insurance Co.	125,000	594,945	719,945
† 36. Oakland Motor Car Company	700,000	.....	700,000
37. B. F. Goodrich Company	700,000	.....	700,000
38. American Radiator Company	.....	667,685	667,685
* 39. Clicquot Club Company	650,000	.....	650,000
Carried Forward	27,365,000	22,524,738	49,889,738

	In Newspapers (*See Note 1*)	In Magazines (*See Note 2*)	Total
Brought Forward	$27,365,000	$22,524,738	$49,889,738
40. Pond's Extract Company.....	200,000	445,100	645,100
41. General Cigar Company.....	600,000	.....	600,000
42. Valentine & Company.....	.....	595,500	595,500
43. Cudahy Packing Company.....	.....	592,000	592,000
44. Union Pacific System	570,000	.....	570,000
45. General Electric Company.....	.....	562,140	562,140
46. Rickenbacker Motor Company..	560,000	.....	560,000
47. Radio Corp. of America.....	250,000	303,460	553,460
48. Fels & Company.....	.....	539,350	539,350
49. Cream of Wheat Company.....	.....	525,400	525,400
50. Simmons Company	210,000	308,960	518,960
51. Macfadden Publications	510,000	.....	510,000
* 52. Lehn & Fink, Inc.....	.....	504,410	504,410
53. Fleischmann Company	.....	503,560	503,560
54. Atchison, Topeka & Santa Fe RR	500,000	.....	500,000
55. Literary Digest	500,000	.....	500,000
56. Standard Oil Co. of California..	500,000	.....	500,000
57. Calif. Fruit Growers Exchange.	180,000	313,550	493,550
* 58. Coca-Cola Company	170,000	322,650	492,650
59. Royal Baking Powder Company	175,000	312,990	487,990
60. California Packing Company...	.....	484,860	484,860
61. Bon Ami Company.....	.....	462,350	462,350
* 62. International Silver Co.....	.....	459,690	459,690
63. Jell-O Co., Inc.....	.....	458,200	458,200
64. Southern Cotton Oil Trading Co.	175,000	280,776	455,776
65. Canada Dry Ginger Ale, Inc....	450,000	.....	450,000
66. Famous Players-Lasky Corp....	150,000	298,500	448,500
67. Pro-phy-lac-tic Brush Co.....	.....	413,181	413,181
68. Brunswick-Balke-Collender Co...	400,000	.....	400,000
69. Edna Wallace Hopper.....	400,000	.....	400,000
* 70. Texas Co.	.....	395,500	395,500
71. Fuller Brush Company	.....	392,450	392,450
72. Hudson Motor Car Co.....	.....	387,270	387,270
73. Oneida Community, Ltd.....	.....	385,575	385,575
74. Pompeian Laboratories	.....	382,250	382,250
75. Gold Dust Corp.....	.....	379,570	379,570
76. Packard Motor Car Co.....	.....	354,425	354,425
77. Salada Tea Company.....	350,000	.....	350,000
78. Shredded Wheat Company	350,000	.....	350,000
79. Crane Company	.....	342,600	342,600
80. National Carbon Company.....	340,000	.....	340,000
81. Cadillac Motor Car Co.....	.....	338,870	338,870
82. R. L. Watkins Co.....	.....	335,452	335,452
83. Libby, McNeil & Libby.....	.....	335,100	335,100
84. Maxwell Motor Corporation....	.....	325,500	325,500
85. Du Pont de Nemours & Co., Inc.	.....	325,240	325,240
86. Firestone Tire & Rubber Co.....	.....	324,800	324,800
87. Hoover Co.	.....	323,700	323,700
88. Fisher Body Corporation.....	.....	320,100	320,100
89. Standard Oil Co. of New York..	.....	311,505	311,505
90. Armour & Co.....	.....	301,200	301,200
91. Anheuser-Busch, Inc.	300,000	.....	300,000
92. Auto Strop Safety Razor Company	300,000	.....	300,000
93. Cheek-Neal Coffee Company....	300,000	.....	300,000
94. Hurley Machine Co.....	300,000	.....	300,000
95. Portland Cement Association...	300,000	.....	300,000
96. Union Oil Co. (Los Angeles)...	300,000	.....	300,000
Carried Forward	36,705,000	37,472,472	74,177,472

	In Newspapers (*See Note 1*)	In Magazines (*See Note 2*)	Total
Brought Forward	$36,705,000	$37,472,472	$74,177,472
97. General Motors Co.	.....	288,300	288,300
98. Kroehler Mfg. Co.	.....	283,900	283,900
99. Zonite Products Co.	.....	282,870	282,870
100. Chrysler Motor Corporation	.....	281,100	281,100
101. Nordyke & Marmon Company	280,000	.....	280,000
102. Washburn-Crosby Co.	.....	279,250	279,250
103. E. R. Squibb & Son	.....	278,460	278,460
104. International Magazine Co.	275,000	.....	275,000
105. Aluminum Cooking Utensil Co.	250,000	.....	250,000
106. Barrett Company	250,000	.....	250,000
107. C. F. Mueller Company	250,000	.....	250,000
108. National Biscuit Company	250,000	.....	250,000
109. New York Central Lines	250,000	.....	250,000
110. Parker Pen Company	250,000	.....	250,000
111. Maytag Company	225,000	.....	225,000
112. Boyce & Veeder Company	220,000	.....	220,000
113. Associated Oil Co. (San. Fran.)	200,000	.....	200,000
114. Certain-teed Products Co.	200,000	.....	200,000
115. Johns-Manville Company	200,000	.....	200,000
116. Phenix Cheese Company	200,000	.....	200,000
117. Royal Typewriter Company	200,000	.....	200,000
118. Vick Chemical Company	200,000	.....	200,000
119. Alfred H. Smith Co. (Djer-Kiss)	200,000	.....	200,000
120. Williamson Candy Company	200,000	.....	200,000
121. Calif. Prune & Apricot Growers	180,000	.....	180,000
122. A. Stein & Company	180,000	.....	180,000
123. W. & J. Sloane	170,000	.....	170,000
124. Cunard Line	160,000	.....	160,000
125. W. L. Douglas Shoe Company	160,000	.....	160,000
126. Holland Furnace Company	165,000	.....	165,000
127. Northern Pacific Railway Co.	160,000	.....	160,000
128. Bauer & Black	150,000	.....	150,000
129. Dairymen's League Co-op. Assn.	150,000	.....	150,000
130. W. A. Sheaffer Pen Co.	150,000	.....	150,000
131. American Express Company	125,000	.....	125,000
132. French Lick Springs Hotel Co.	125,000	.....	125,000
133. Phoenix Hosiery Company	125,000	.....	125,000
134. The Western Company	125,000	.....	125,000
135. C. Brandes, Inc.	100,000	.....	100,000
136. Florida Citrus Exchange	100,000	.....	100,000
† 137. Indian Refining Company	100,000	.....	100,000
138. Lalance & Grosjean Mfg. Co.	100,000	.....	100,000
139. McCall's Magazine	100,000	.....	100,000
140. Shell Oil Co. (Los Angeles)	100,000	.....	100,000
Grand Total	$43,530,000	$39,166,352	$82,696,352

Note 1: Estimates compiled by the Bureau of Advertising of the American Newspaper Publishers Association.

Note 2: From a statistical study of 30 magazines by Crowell Pub. Co.

* For names indicated in this manner, *Printers' Ink* has on its records the amount of the original advertising appropriations. The records show the first appropriations made by the companies thus indicated to be as follows: Armstrong Cork Company, $3,000. Borden Sales Company, Inc., $513.75. Campbell Soup Company, $4,264. Clicquot Club Company, $10,000. Coca-Cola Company, $73.96. Hupp Motor Corporation, $100.68. International Silver Company, $10,000. Lehn & Fink, $5,000. Postum Cereal Company, $1,669.84. Procter & Gamble Company, $11,543. Texas Company, $8,000. Vacuum Oil Company, $90,000. Wm. Wrigley, Jr., Company, $32.

† Dealers' advertising included in these newspaper figures.

This compilation does not, of course, include the total advertising expenditure of the concerns listed. It represents their expenditures in only thirty magazines to begin with, and includes none of their expenditures in the other general magazines, farm papers, theater programs, direct-mail, window-displays, novelties, premiums, motion pictures, slides, directories, signs, and other mediums.

BRAND SPECIFICATION

An excellent statement concerning the purposes for which all this money is spent is made in an advertising trade paper:[4]

In the statement to its stockholders issued recently by The American Sugar Refining Company, we find this statement:

"Formerly, as is well known, household sugar was largely of bulk packing. We have described the sale of package sugar and table syrup under the trade names of 'Domino' and 'Franklin' with such success that the volume of trade-mark packages now constitutes roundly one-half of our production that goes into households.

"This package development necessitated very large changes both in equipment and in refineries. The advantage of this business is its direct contact with the consumer."

There are two significant points in this brief statement. First, that the advertising and sales effort put behind this company's packaged sugars has resulted in selling approximately half of its volume in package

[4] *Advertising and Selling Fortnightly*, February 25, 1925, p. 27.

form, whereas only a few years ago all sugar was sold in bulk. Second, that although the packaging operation involved a large outlay for equipment and changes in plant, this has been compensated for by the greater control the company has over its business through direct contact with the users of its product.

These facts should be of vital interest to any executive who faces the problem of marketing a staple product that is hard to control because it is sold in bulk.

Twenty years ago the sale of sugar in cardboard cartons under a brand name would have been unthinkable. Ten years hence this kind of history will have repeated itself in connection with many other staple commodities now sold in bulk, both to the householder and to the industrial consumer.

Perhaps the most authoritative brief statement of the manner in which brand specification has attained its present proportions is contained in the report of the Joint Commission of Agricultural Inquiry on Marketing and Distribution,[5] and follows here:

Under liberal governmental laws, fostering educational opportunity, monthly and weekly magazines and papers of wide circulation came into existence about 1880 and increased rapidly in number until about 1910. These magazines offered an opportunity for wide exploitation of manufactured goods. However, to realize a profitable return on advertising, it was necessary for

[5] Page 116, "Marketing and Distribution," Report of the Joint Commission of Agricultural Inquiry.

the makers of goods to identify their products and guarantee satisfaction.

This led to increased branding and trade-marking of goods and packaging of foodstuffs. With the opportunity offered through widespread circulation of advertising mediums, there developed broadcast distribution of goods and a competition between manufacturers of parallel articles for national markets. This competition reflected itself in a further effort on the part of manufacturers to improve methods of manufacture and secure economies of large volume production. Competition was not confined, however, to production, but extended to the purchase of more advertising space in a larger number of publications and an increased selling effort of most intensive character.

In addition to the usual selling organizations calling upon the wholesalers, manufacturers organized specialty selling, in which they employed men to call upon retailers, distribute samples, and utilize such devices as would tend to compel retailers to purchase goods through the wholesaler. Each new selling device was adopted by competitive manufacturers, with the result that the distribution of manufactured goods became a competition of spending, until it developed a burden of distributive costs in excess of the value of the commodities distributed. However, consideration should be given to the fact that in the competition of identified goods there has developed a greater excellence, uniformity, convenience, hygienic protection of foodstuffs and a radical change in the living habits of the American people. It is apparent, however, that these advantages do not sufficiently compensate for the disproportionate cost of the distribution of necessities.

Brand specification, as the term is used by advertising men, describes the habit of buying by specifying a brand. Standard specification, on the other hand, may be described as the specifying of established standards in buying. Brand specification is so easily confused with standardization and standard specification that it comes as somewhat of a shock to realize that they are really diametrically opposed.

There is a difference between the branding of a product and what advertising men call brand specification.

Brand specification is really an abuse of branding.

Branding itself is merely a means of making it possible to identify the maker of a product. When used on products manufactured to standard specifications, it makes it possible for the buyer to determine what makers conform or fail to conform to standard. But when branding is used primarily to make it possible for a manufacturer to create brand specification through national advertising, it serves fundamentally to enable the manufacturer to evade or lessen price competition.

An excellent illustration of how brand specification lifts a product out of competition is furnished by one national advertiser of a basic material. In 1914 the American Rolling Mill Company started national advertising to persuade the users of a certain kind of iron to specify

"Armco," as the iron to be used in their castings. An article describing this campaign was very suggestively entitled, "Advertising Lifts Armco Iron Out of Rut of Raw Materials."[6] This article describes the reactions of dealers to this campaign, and among others, it quotes the remark of one buyer as follows: "We do not care a continental about your product, although it is all right no doubt, but we do care about your advertising." In other words, the campaign to bring about brand specification in this iron resulted in making this dealer ignore the intrinsic value of the merchandise and to buy it merely because the customers he served were specifying "Armco."

Quite without regard to whether this particular manufacturer took advantage of the opportunity to exploit the market for his product, in so far as price is concerned, it is necessary to recognize that such an opportunity existed. Human nature being what it is, few manufacturers refuse to take advantage of such opportunities. Hundreds of manufacturers who have succeeded in persuading the public to specify their brands have taken advantage of it. Higher prices have enabled them to meet the cost of the national advertising, the excess cost of high pressure marketing as compared with ordinary marketing, and earn profits over and above those normal in the field in which they operate.

It is evident therefore that what distinguishes

[6] *Printers' Ink*, February 25, 1915.

national advertising economically from retail advertising and from other kinds of advertising such as financial advertising, industrial advertising, and trade advertising, is the fact that by enabling the manufacturer to create an artificial demand for his particular brand, the manufacturer can secure higher prices than he could command if his product were sold purely and simply as merchandise at prices fixed by the fluctuations of supply and demand.

XVI

HIGH PRESSURE CREDIT

Whenever a product is sold—whether the seller be manufacturer, wholesaler, or retailer—on other than a cash basis, the seller is engaged in selling not only merchandise, but also credit. Credit is something which should be sold, in the interest of general economy, only by those in the business of banking. Whenever credit, especially long credit, is offered, apparently "free," to persuade someone to buy, it adds an item of expense to the cost of marketing the far-reaching importance of which is not generally recognized.

Fortunately, reckless credit given as a means of promoting sales is so obviously filled with danger, that except in the case of installment selling, it has as yet few defenders. Yet it is an amazing commentary on the times that a well known accountant [1] writing in a business journal should in all seriousness have urged this kind of high pressure credit as the solution of the troubles of some of those manufacturers who are confronted with imperious need for increased sales.

[1] William R. Basset, "Selling Where the Profits Are," *Advertising and Selling Fortnightly*, August 12, 1925.

Consider, for example, a concern which for years had been very rigid in its credit policy. A great many of the contractors who are the users of the commodity which it makes have no credit rating and are notoriously poor business men. The concern absolutely refused to sell to them, overlooking the fact that some one—probably a competitor—was supplying their needs.

This concern's product was sold at a gross profit of 30 per cent on the selling price.

A very careful study of the market which was shut out because of a determination to keep credit losses below 1 per cent showed several interesting things. One was that by lowering the bars to the point where only $4 out of every $5 of the new business was reasonably sure to be collected, an additional volume of $500,000 would be secured with no additional selling cost. In other words the credit department had been refusing one-ninth of the business which the existing selling force could sell although 80 per cent of what was turned down could probably be collected. The company had been doing a business of $4,000,000 at a selling cost of $1,200,000. Even though bad debts on the extra $500,000 amounted to 20 per cent, the company's net profits would increase $100,000.

The suggestion that this policy be followed brought forth terrible wails from the credit department and the treasurer. The sales department was for the idea from the start and in time, the owners decided that an extra $100,000 in dividends was more to be desired than a self-satisfied credit department.

Pride in the ability to keep losses low is sometimes very costly. It is entirely possible to eliminate bad debts

entirely by the simple procedure of refusing to sell anything to any one. Ridiculous you say? Only in degree. As long as net profits can be increased what difference does it make what the credit losses amount to?

What difference does it make? Mr. Basset challenges the world to produce a reason for refusing to debase the standards of credit giving. Only one need be furnished. If competition between manufacturers is based upon liberal—I prefer to call it reckless—credit giving, it results in keeping in trade a host of parasites who ought not to be in the business either because they are dishonest or inefficient or both. The man who advocates the extension of reckless credit must be a man so obsessed with the mania to sell, that the general welfare of his own industry and of business in general is of absolutely no interest to him.

But if this kind of high pressure credit is without a really dangerous number of advocates, there are a legion of advocates for high pressure credit in the form of installment selling. What is more, most of those who are its advocates are also its practitioners. It has proved to be an effective means of stimulating the ultimate consumer to buy what otherwise he could not buy so quickly, —to stimulate buying by mortgaging future income. So today we are having an orgy of installment selling, to the tune of "after us the deluge!"

What a change since Pollonius said, "Neither a borrower nor a lender be."

At the time this is being written there are six hundred time payment finance corporations which take care of the installment payments for purchases of automobiles, and new finance corporations are being organized daily.* A single concern selling diamonds and jewelry on the installment basis, numbers 300,000 customers. A check-up of twenty-seven newspapers in fifty-seven cities between November 11 and December 20, 1923,[2] showed 141 advertisements which made a direct appeal for time payment sales on the following products:

Furniture	Sewing Machines	New Autos
Pianos	Women's Apparel	Typewriters
Used Cars	House Furnishings	Diamonds
Clothing	Safes	Vacuum Cleaners
Washing Machines	Radio Equipment	Lamps
Stoves	Violins	Candy and Nuts
Rugs and Carpets	Cedar Chests	Gifts
Jewelry	Silverware	Trucks
Phonographs	Kitchen Cabinets	

This is by no means a complete list of the products sold on the installment plan. Some of the more amazing developments of this phase of high pressure marketing include the following: house

* A year after this was written, Clarence Y. Palitz, president of the Credit Alliance Corporation, made a survey of installment selling and estimated that there were more than 1,500 organized finance companies, and more than 2,500 individuals dabbling in the finance business.

[2] *Printers' Ink,* February 1924.

paint to home owners; ice and coal to stimulate buying in the off season; summer and winter vacations; automobile. insurance; plumbing fixtures; convention expenses; ready-cut houses; tours on the "travel now and pay later" plan. The future development of this phase of marketing is evidently charged with unlimited possibilities.

In 1915 and 1916 when the business of selling automobiles on the installment plan was first introduced, it met with bitter hostility on the part of many of the most influential men in the automobile industry. The "pay as you ride" policy had to fight for an opportunity to show what it could do. Automobile manufacturers of those days considered the policy of selling for cash only, which had prevailed up to that time, very largely responsible for the growth of the industry, since it gave the infant industry cash resources at a time when ordinary bank credits were difficult to secure. It was generally predicted that once the time payment plan was introduced, the used car problem would multiply to a point which would enormously increase the cost of selling. At that time, time payments may be said to have been zero. By 1920, the General Motors Acceptance Corporation, which handled all the installment business of the Chevrolet, Buick, Oakland, Oldsmobile and the Cadillac automobile companies, reported approximately 50 per cent. of sales on the installment plan. Today it is estimated that over 85 per cent. of all of the automobiles

which are sold are sold on the time payment plan.

According to the National Automobile Chamber of America reports, it is estimated that the retail value of automobiles purchased and sold in this country in 1923 was approximately two and one-half billion dollars. If 85 per cent. of these sales were made on time payments, $2,125,000,000 worth of automobiles were sold in that way.

During the antebellum period when installment selling had not yet taken its first steps towards respectability, it was very largely confined to sewing machines, books, furniture, and pianos. The business was very largely in the hands of unscrupulous canvassers and unprincipled retailers. The entire business was saturated with deceitful advertising, untruthful salesmanship, and bull-dozing collection methods. It has since that time changed its outer habiliments. But its underlying economic nature has not changed.

Installment selling, which originally was a rather unscrupulous method used only by the "shysters" of trade, has now been taken over by "big business." It has been systematized, organized, and made respectable.

Modern methods have furnished installment sellers what they badly needed: a respectable facade for houses of organized usury. One study [3] of installment selling proves this by calling attention to the fact that—

[3] "The Arguments For and Against Instalment Buying," by Q. F. Walker, economist for R. H. Macy & Co., Inc., New York City.

Most installment selling plans compute interest on the aggregate cost of the article and do not charge interest at a fixed rate on a decreasing balance of payment. The result is that the interest charges on such purchases often aggregate 25 to 30 per cent or more. The customer is never told the plain truth about the interest cost in his purchase.

Balance Payable in	Rates Finance Company Say They Charge	As It Actually Figures	Total Cost of the Credit to Consumer
4 months	4%	22.32%	48.00%
5 months	4½	21.04	40.00
6 months	5	20.16	34.27
7 months	5½	19.52	30.00
8 months	6	19.03	26.66
9 months	6½	18.68	24.00
10 months	7	18.40	21.81
11 months	7½	18.18	20.00
12 months	8	18.00	18.45
Average	6%	19.48%	29.24%

People who twenty years ago would have scorned to purchase anything for which they could not pay, and who looked upon such methods of buying as befitting only the ignorant or improvident, today buy bigger homes, bigger automobiles, and even bigger radio receivers than they have the money for which to pay.

The tragedy of the appeal to buy on the basis of credit can be expressed in one word, "overbuying." The victims of this tragedy are the owners of books that are not read, pianos that are not played, and phonographs, radio receivers,

automobiles, and even homes, the installments on which are a perpetual tragedy.[4]

The American Surety Company made an analysis to determine the chief causes for moral lapses on the part of defaulting employees—for which lapses, up to the face of the policy, the American Surety Company undertakes to indemnify employers. With such a practical problem before him, it is probable that the investigation of B. J. McGinnis, manager of the Claim Department, was a thorough one and that its conclusions are worth listening to:

"It has been evident for some time that defalcations by employees handling money and securities are on the increase. . . . It is clearly shown by our reports that there are several ruling factors which cause men to become dishonest. Fashions change in crime as they do in medicine and in other fields, and so do inciting reasons. Today the desire to own an automobile or a large car, it is revealed by our studies, lies at the bottom of the peculations of many employees—whereas a few years ago racetrack gambling stood among the leading causes of 'inside' theft. It is not always the joy-rider who steals either—it is often the young married man whose wife insists upon having a car in addition to a fur coat, platinum jewelry, and all the luxuries of modern life."

Mr. McGinnis pays his respects to installment buying. He recites the case of one defaulter whose rent and installment payments on an automobile ALONE equaled his salary. In addition he was purchasing a fur coat and jewelry for his wife, and

[4] *The Nation*, May 19, 1926.

"has enough extra to make a social hit in the neighborhood. . . . Changed standards of living are often responsible for peculations. Defaults are not always DUE to economic pressure (of sheer poverty) but to a desire to live in a luxurious way and impress the neighbors. Luxuries are born faster today than ever before, and every one of them can be bought 'on time.' "

In a book dealing with economics, the tragic aspect, since it affects only the consumer, must be subordinated to the economic aspect. What concerns us directly, therefore, is the possible effect of this flood of installment selling upon the general prosperity.

Sewing machines, one of the first items to be sold by high pressure marketing methods, in which installment selling, house to house canvassing, and advertising are all used, are sold by intensive campaigns which cover every street and road in the civilized world—and much territory not really civilized. Ten to twelve per cent. of the machines sold are returned, but losses on bad debts are only 2 or 3 per cent. of sales. Contracts, however, sometimes run two and three years. Some glimmer of what this costs the consumer of sewing machines may be gleaned from the fact that sewing machine companies allow a 20 per cent. discount for cash and consider 30 days as cash. If sewing machines were marketed on some less extravagant and wasteful plan, the consumers would have at least 25 per cent. and perhaps as much as 33 1-3 per cent. of all that is spent for sewing machines with which to purchase other things.

The furniture business and the business of selling pianos, owing to the ignorance of consumers as to values, lend themselves to installment selling almost as well as the business of selling deluxe books. Mark-ups have to be above 100 per cent. in order to make the installment furniture business safe and profitable. In the installment book business mark-ups are apt to be 500 per cent. A set of books which costs $10 to manufacture is usually sold on the installment plan for $50.

A great variety of costs beginning with the losses on bad debts make these extravagant margins necessary.

The systematizing of installment selling today has not resulted in any more scientific selection of risks. The loss on bad debts is substantially the same as in the past. Modern methods have merely produced a larger scale of operations and enabled installment sellers to distribute the risks so widely that strict credit checking has become a short-sighted policy. The additional profit to be secured by selling surplus production to the more hazardous classes of debtors is weighed against the probable total increase in bad debts, and if the estimated losses are less than the estimated increase in profit, the greater hazard is disregarded.

While the loss on bad debts is often kept down to small amounts, as little as 1 per cent. being quite common, this is probably the smallest item of cost involved. For instance, one furniture house estimates its losses on bad debts as 4 per

cent.; its cost of collecting 4 per cent.; its cost of accounting 3 per cent.; and its cost of investigating ½ per cent.

Another very large addition to the installment costs comes with selling. Salesmen have to be paid regularly each week, or as sales are made. Salaries and commissions have to be paid promptly. But in the installment business they are not earned until the installments are fully paid. The result is that the manufacturer or retailer operating on the installment plan has to invest large sums for selling expenses in addition to laying out the cost of the merchandise. With this comes a special kind of loss peculiar to installment selling, for whereas the installment house may recover some portion of its accounts by taking back the merchandise when the customer defaults, it rarely recovers what it pays out in commissions and salaries on defaulting accounts to salesmen who have left it for other employment.

Then there is the cost of the capital used in the business. But for the fact that it still takes a large amount of capital, and used to take a very much larger amount of capital to conduct the installment business, scarcely anybody in the country would do business on a cash basis. Many of the failures in the installment business have been due to insufficiency of capital. This has contributed not merely to the failure of local retailers, but to that of many large corporations, both those selling products like phonographs to the general

public and those selling machinery for use in agriculture and factory production. The capital necessary to conduct an installment furniture business is figured variously from one and one-half times as much as a cash business, to five times as much. This capital is tied up and not only has the cost of carrying it to be paid for, but also the cost of collecting it in dribs and drabs from the customers.

Before summing up, let me quote upon this subject one of the country's most far-sighted business men. In 1926 Senator James Couzens of Detroit made the rather dramatic announcement that he was "discontinuing at once" his business of making electric refrigerators because of the practice of installment selling. It was installment selling that was to blame for that drastic step, said Senator Couzens.

There are economic laws that none of us can safely break. The electrical refrigeration industry has mortgaged itself to the installment system, and in my estimation it is being seriously misused. Installment selling methods are being permitted to fasten themselves upon industry in general, and it has yet to weather the storm which inevitably follows such practices.

I personally refuse to sacrifice what experience has taught me are basic principles, for sales methods that attempt to justify the sale of the product through "thirty-day trial offers" and "down payments" as low as 2 per cent—with two years to pay the balance.

The aim of this company was to build a low-priced

unit for the average home. We had built, and were on the verge of announcing, this machine when the present decision was reached. Even with a low-priced unit it appears futile to continue in view of the sales methods existing in the industry. For as rapidly as the manufacturer reduces his costs and prices, the dealer, through circumstances forced upon him by the installment believers, adds "installment charges" to the list price. He does this because, to compete on two-year payment terms, he must protect himself on the maintenance and service expense loaded upon him by the customer who has bought on unreasonably long terms.

Thus the customer pays for America's wide spreading installment system.

There are six outstanding points in connection with installment selling:

1. The installment method of selling has increased steadily since its introduction in the furniture and book fields and much more rapidly both in volume and in variety of products during the last few years.

The Department of Domestic Distribution of the United States Chamber of Commerce [5] estimated that 17 per cent. of all goods sold at retail in 1925 was paid for on the installment plan. This indicates a volume of installment business of from six to seven billion dollars per year.

2. The time payment plan is really a form of anticipating normal sales. The immediate effect of anticipating normal sales is to unduly stimulate

[5] *Women's Wear*, March 26, 1926, p. 8.

investment in production facilities, and the ultimate effect is to curtail buying by the consumer until income has caught up with debt.

3. It results in a reduction in sales for cash and an increase in sales on credit, and thus very considerably increases the cost of distributing all goods. The total consumption of goods is reduced and income which might have been expended for merchandise is really dissipated in carrying costs.

4. The rate of depreciation on many kinds of goods is more rapid than the rate of payments upon them. In some cases the consumer actually has to continue paying for merchandise long after it has been consumed. This fact not only lessens the security back of the credit, but it demoralizes the debtor and reduces the earning capacity of those who habitually buy in this way.

5. The cost of handling the unprofitable accounts is naturally shifted to those who do pay their installments, and they pay proportionately more for their credit. Thus we have really a system of selling which operates to burden those honest but thoughtless persons who do not see that what they are really doing is paying for the extravagances of those who dishonestly buy on the installment plan.

6. Those who offer time payments compete with each other on liberality of terms rather than on quality and price of merchandise.

Any competition not founded on quality, service, or price is demoralizing and dangerous to those

who engage in it. Cash selling does not favor the dishonest at the expense of the honest—it does not burden the thrifty because of the extravagance of the wasteful. Credit selling, regardless of whether it is done by a concern doing part cash and part credit business, or all installment business, always burdens those who do pay with the costs of losses for selling to those who do not.

XVII

HIGH PRESSURE CAPITALIZATION

As recently as 1914, when the B. F. Goodrich Company of Akron, Ohio, included an item of $57,000,000 for goodwill, patents, and trade-marks as a basis for the capitalization of the company, conservative bankers indulged in widespread criticism of this as an uneconomic and unsound business procedure.

The criticism was based upon the assumption prevalent in the banking and investment world of that time that only tangible assets were properly capitalizable by industrial corporations. But the criticism incidentally showed that a complete misconception existed as to what actually was being capitalized. The bankers assumed that it was goodwill of the kind then most generally associated with that term. As a matter of fact, what was capitalized was an entirely new kind of goodwill—a thing different from the old in its genesis and its effect although easily confused with the old because of the similar nomenclature. The new goodwill acquired a standing and respectability to which it was not entitled by the simple process of taking over the name of the old goodwill

which it in so many instances completely eclipsed in aggregate value.

What is the "new" and what is the "old" goodwill? And in what way does the capitalization of the new add to distribution costs while the capitalization of the old fails to do so?

A good definition of what I call the old goodwill is contained in the judgment of the court in the case of Washburn v. National Wall Paper Company, (81 Federal Rep. 20):

> When an individual or a firm or a corporation has gone on for an unbroken series of years conducting a particular business, and has been so scrupulous in fulfilling every obligation, so careful in maintaining the standard of the goods dealt in, so absolutely fair and honest in all business dealings that customers of the concern have become convinced that their experience in the future will be as satisfactory as it has been in the past, while such customers' good report of their own experience tends continually to bring new customers to the concern, there has been produced an element of value quite as important—in some cases, perhaps, far more important, than the plant or machinery with which the business is carried on. That it is property is abundantly settled by authority, and, indeed, is not disputed. That in some cases it may be very valuable property is manifest. The individual who has created it by years of hard work and fair business dealing usually experiences no difficulty in finding men willing to pay him for it if he be willing to sell it to them.

It will be seen that the goodwill of which the court spoke involves years of good conduct which include (1) fulfillment of contracts; (2) maintenance of standards in the product; and (3) absolute fairness and honesty. This kind of conduct by a concern creates great confidence in it among its existing customers and a trade reputation which attracts a stream of new customers. It is not essential to the creation of this kind of goodwill that the product of the company be patented or trade marked. If the conduct of the company or the quality of its product creates a "clientele" for it, it has the old goodwill.

The new goodwill distinguishes itself from the old primarily by virtue of the fact that it does not come into existence in the same way; in that (1) it is not dependent upon years of "good" conduct, (2) does not require scrupulous fulfillment of contract, nor (3) absolute fairness and honesty in business. The two kinds of goodwill may come and in many cases do come into existence at the same time, but the old exists as a very valuable asset in many firms which have never developed any of the new goodwill, while many firms have developed very valuable high pressure goodwill without undergoing the discipline and practicing the conduct essential to the creation of the old goodwill.

The new goodwill is solely and simply the excess over normal profit which is earned by the sale of products through high pressure marketing. It is

this capacity for earning excess profits and not the old goodwill which is being used increasingly as a basis for the goodwill capitalization which is conspicuous in present day finance.

Goodwill based upon the confidence of customers and goodwill based upon high pressure marketing are two different things. The one is created without adding to the cost of distributing the product —the other can only be created by adding to it.

The new goodwill is not something which inheres in an individual or in an organization—it can hardly be said to inhere in a product—it is something which develops from high pressure exploitation of a name or brand. It exists only in conjunction with brand specification. It comes into existence only by creating consumer demand for one brand as compared with one or more competing products.

The natural consequence of the discovery of the limitless possibilities of the new goodwill has been a decline in the relative importance attached by the business world to the technique of production in favor of the technique of marketing. If efficiency in marketing and advertising builds capitalizable goodwill more rapidly than efficiency in production, then effort and expenditure is naturally devoted to more and better sales promotion rather than to greater and more efficient production. This peculiar inversion of the normal economic process is made clear in some testimony

of Roger W. Babson before a congressional committee in 1918:

> For instance, I have in mind a man who owns some asbestos land. This land is worth little or nothing. The question came up as to whether he should get an engineering expert to develop that land and take his chances on selling the product, or whether he should get an advertising expert to create a demand for that product and then prepare to develop the property. In the first place, if he takes the money and uses it and gives it to the engineer and lets him hire day laborers to work up that proposition, he can charge those expenses to invested capital, and they are recognized by you as invested capital. If, however, he gets a publicity man and uses that money to develop a market for the product, then that is handled and treated by you on an entirely different basis.[1]

Mr. Babson makes the customary assumption of those who are interested in promoting the idea of capitalizing goodwill—that demand for a product will not develop unless it is created by some form of high pressure selling. He assumes that an investment of money for the development of asbestos land and an investment of money for advertising to create a demand for asbestos are true alternatives. As a matter of fact, they are not alternatives at all. Even after the making of an investment for the creation of the demand, an investment for the development of the land still has to be made. The real question is whether the

[1] Reported in *Printers' Ink*, July 25, 1918.

two investments are truly analogous—whether the advertising should be treated as an incidental expense or whether it should be included in the capitalization as an investment in publicity upon which dividends should be paid precisely the same as an investment in land or factories. If the advertising is normal in volume; if it is merely a selling expense, no investment in it is necessary for the cost of the advertising is then paid out of income like any other expense. On the other hand, if it is proposed to really invest money in advertising; to spend more money in advertising than can be secured from current sales; then it is obvious that prices must be raised sufficiently to furnish the additional profit to pay interest and dividends upon the capital invested in advertising.

One of the most succinct statements of this doctrine is that made by a well known advertising agent, Clarence D. Newell, president of the Newell-Emmett Company, Inc., New York.[1]

> Advertising may be considered both as a method of business and as a productive service to business.
>
> Advertising as a method of business has for its objective the increase of sales volume.
>
> Its cost may be added to current selling expense in the belief that such addition will increase profit to a greater degree than it increases expense. Or it may be invested out of capital or surplus in the belief that at some future time it will yield a profit on that investment.

[1] *Advertising and Selling Fortnightly*, November 3, 1926.

The capitalizing of goodwill created through advertising is the subject matter of a book called "Trade-Mark Advertising as an Investment," by Arthur Acheson. I quote one typical case which Mr. Acheson describes in his book.[2]

Some years ago a certain breakfast food concern bought up a number of mills making and advertising competing brands of food. They then allowed all but one of these brands to die, concentrating much of their advertising upon this one brand. At the time of this combination, all of the tangible assets of the new organization could easily have been reproduced for about a million dollars. They capitalized the new concern for three and one-half millions dollars, the excess above a million representing old trade-mark values. At the end of a comparatively short term of years, while the value of the tangible assets of this company had increased to about three million dollars, the company was recapitalized for twelve millions. The president of the company, at that time, over his own signature, in a daily paper, stated that the profits on their one advertised brand in the preceding year, would pay six per cent on a capitalization of fifteen million dollars. Taking their tangible assets then at three million dollars, the nine millions represented what they considered the capitalizable value of their accrued advertising. The bulk of this nine million dollar value had been built up in a period during which not over half this amount had been expended in advertising. This is not a unique case; a number of such and even greater growths in the

[2] Pages 11-12-13, "Trade-Mark Advertising," *New York Evening Post*, 1917.

capital value of brands have been made in the past twenty-five years.

Some idea of the extent to which the new goodwill has been capitalized by national advertisers can be secured from the following list giving the amount of goodwill shown by their balance sheets:

		Goodwill
American Chicle Co.	1924	$ 8,766,099
Ward Baking Corp.	1924	11,383,413
Goodyear Tire & Rubber Co.	1924	12,500,000
R. J. Reynolds Tobacco Co.	1924	1,319,091
Continental Motors	1923	5,908,316
Borden Sales Co.	1923	5,942,876
Hartman Corp.	1923	4,992,992
Corn Products Refining Co.	1923	16,000,000
Shredded Wheat Co.	1922	4,500,000
Fisher Body Corp.	1924	3,268,340
General Motors	1923	22,440,811
William Wrigley Jr. Co.	1923	6,000,000
V. Vivaudou, Inc.	1922	6,772,975
Hupp Motor Co.	1922	3,858,920
Simmons Co.	1922	2,430,479
Liggett & Myers	1922	40,709,711
Pierce Arrow Motor Car Co.	1922	5,000,000
General Cigar Co.	1922	19,326,000
Julius Kayser & Co.	1922	5,644,000
Torrington Co.	1922	1,923,697
Cluett Peabody & Co.	1922	18,275,000
P. Lorillard Co.	1921	21,137,927
Coca-Cola Co.	1921	24,966,230
Stewart-Warner Speedometer Corp.	1920	9,188,433
American Cotton Oil Co.	1920	23,594,869
Pyrene Mfg. Co.	1918	1,002,450
American Tobacco Co.	1918	54,099,430
Tobacco Products Corp.	1914	2,000,000
B. F. Goodrich Co.	1913	57,000,000
Onyx Hosiery Co.	1913	1,500,000

This list is by no means complete, even as to those carrying the largest amounts, but it is sufficient to give the reader an idea of the extent to

which the capitalizing of goodwill has been incorporated in modern business practice.

Some of the corporations which earn the very largest sums from profits based upon goodwill are not included in the above list.

For every corporation which includes in its financial statements the value of its goodwill, there are probably a dozen corporations which list goodwill at $1 or which carry no item to represent it at all. In these cases goodwill has been written off, surplus credited, and generally large stock dividends paid. When written off, a secret reserve results. But whether the goodwill is carried on the balance sheet at its true value, or whether it exists merely as a secret reserve, in either case the company has to earn profits over and above that which might be considered normal.

The most modern method of capitalizing goodwill uses the device of a no-par stock corporation. Incorporation as a no-par stock corporation has for national advertisers the inestimable advantage of making it very easy to issue stock in unlimited amounts purely upon the earning power of goodwill—without publishing the fact that the security back of the stock consists principally of goodwill. A recent example may be worth analysis. On March 18, 1826, the stock of the Lambert Company, which was to take over the ownership of 56¼ per cent. of "Listerine" was offered the general public. The company was capitalized as follows:

	Authorized *Shares*	To Be Issued *Shares*
Common Stock (without par value).....	1,000,000	281,250
Deferred Stock (without par value)	100,000	100,000

This stock was offered at $41.75 per share. On this basis, the 281,250 shares of common stock to be issued had a value of $11,742,187.50.

Now what did this $11,742,187.50 represent?

According to Gerard B. Lambert, President of the Lambert Pharmacal Company, the net *tangible* assets of the company were approximately $1,000,000. As the newly formed Lambert Company owned only 56¼ per cent. of the net tangible assets, the $11,742,187.50 represented $562,500.00 of net tangible assets and $11,179,687.50 of "goodwill." This, however, was stock which represented only 56¼ per cent of the "goodwill." The value of the entire "goodwill" on the same basis was therefore $19,875,000.00. Consumers of the company's products therefore pay not only dividends on tangible assets of $1,000,000 but on "goodwill" of $19,875,000, and, of course, all the costs of production, advertising, and distribution.

The advertising history of the Lambert Pharmacal Company is exceptionally interesting. The company was founded 47 years ago. But until 1921, Listerine was marketed with only trifling expenditures for national advertising. It was an "ethical" medical preparation. Then high pressure methods of marketing were adopted. Advertising expenditures jumped by the hundreds of

thousands yearly. By 1925, advertising had increased to over $2,000,000 for the year. The company itself expected it to exceed $3,000,000 in 1926.

What followed is told in the following table:

Years Ended December 31	Net Profits of Lambert Pharmacal Company After Federal Income Taxes at 13½%
1922	$ 724,542.53
1923	1,078,437.31
1924	1,499,210.77
1925	2,011,940.89

This makes ownership of the name Listerine better than ownership of a gold mine. That the exploiters of the name appreciate the fact is demonstrated by their policy of launching new products from time to time, such as Listerine Tooth Paste and Listerine Throat Tablets. The name is plainly going to yield its uttermost farthing of "goodwill."

No one could accuse *Printers' Ink,* the leading trade paper in the advertising field, of overstatement of this subject of goodwill. An editorial in that publication entitled "Selling the Good Will Idea," in the issue of September 23, 1920, paints a beautiful picture of the importance of what I have called high pressure goodwill.

Sell the Good Will Idea. Not many years ago a judge of the Supreme Court of the United States, in a carefully written opinion, characterized a certain business as entirely "advertising begotten." In other words, as he went on to explain, its product was intrinsically

neither superior nor inferior to the product of a host of competitors, and the only distinction which it could claim was the wholly intangible good will toward its trade name which had been fostered by intelligent advertising. That it had gained an annual sale almost equal to the sales of all its competitors put together was due, not to intrinsic superiority, but to the fact that it had been made known to millions of consumers while competing goods, of equal merit, had remained in obscurity.

In brief, if some mighty catastrophe should destroy every vestige of the company's tangible property, it could go on again tomorrow, but if some miracle of oblivion should erase from the minds of the people all knowledge of a certain arbitrary symbol, the business would be gone.

And therein lies the great security of the company's position; that while catastrophes may, and often do, destroy physical property on a large scale, good will is beyond the reach of fire, or flood, or earthquake. Only the slow process of neglect can destroy it.

All of which is neither new nor startling, of course, but it represents a fundamental upon which the advertising men need to tighten their grasp every now and again. Especially today, on the verge of what seems likely to prove a period of trial for the half hearted, weak-kneed advertiser, it is important that this truth should be firmly grasped and clearly set forth.

The time has pretty nearly gone when advertising contracts could be closed on the basis of "13½ pages open; better take 'em quick!" The time is coming when many executives will be wondering whether that advertising appropriation would not look better under

"net profits" in the annual statement than in the pages of the magazines and newspapers. And that is exactly where it will go, in many instances, unless the good will idea is clearly and firmly grasped and understood.

It is a fact, clear and indisputable, that a favorable public opinion is property more valuable than factories or machinery, or even than money in the bank. Once it is created, only neglect can destroy it, but neglect is sure and often swift to destroy. And that which is destroyed is the most valuable property in the world.

The advertiser who understands this, will remain an advertiser and grow bigger. The concern, no matter how large, which fails to grasp it, may well fall from the ranks and grow less. *And the most successful advertising men of the immediate future are likely to be those who can best sell the good will idea!* [3]

The present period of capitalizing goodwill by the issuance of securities based primarily upon consumer demand for branded products is proof of the fact that the selling of the goodwill idea is proceeding along the lines suggested by *Printers' Ink.* Manufacturer after manufacturer is engaging systematically in the business of trying to earn dividends upon what amounts to the efficiency with which he indulges in marketing extravagances. What an appalling situation—that competition, because it has been shifted from the field of quality and price of product to the field of advertising, has apparently become powerless to check the uneconomic marketing methods

[3] *Printers' Ink,* September 23, 1920, p. 170.

upon which the capitalization of high pressure goodwill is based. Apparently the process of inventing new and more effective methods of high pressure distribution, high pressure selling, and high pressure advertising can therefore continue uninterrupted. Apparently high pressure marketing can support itself indefinitely upon the millions of dollars which the investing public will put into corporations which earn dividends by selling branded products at premium prices to a gullible public.

PART III

THE IMMEDIATE PROBLEM

XVIII

THE ELIMINATION OF HIGH PRESSURE MARKETING

I THINK that so far we have established conclusively the truth of four out of the five propositions outlined in the opening chapters of this book—first, that distribution costs in this country, both for physical distribution and for marketing, have risen out of proportion to production costs; second, that high freight rates and cross hauling and unnecessary transportation are principally responsible for the rise in the cost of physical distribution; third, that one of the most important factors in causing the rise in the cost of marketing, as distinguished from the rise in the cost of physical distribution, is "high pressure" selling, "high pressure" advertising, "high pressure" marketing generally; fourth, that manufacturers engaged in mass production and mass selling have been the active factors in the development of extravagant marketing and unnecessary transportation; that they are responsible for the breaking

down of that skillful and skeptical buying by retailers and consumers which tends to raise standards and to lower costs.

I propose now to show that the fifth proposition furnishes a practical and economic technique for eliminating high pressure marketing—that the wastes of high pressure marketing can be eliminated and the cost of distribution lowered if the retailers and wholesalers of the country would, first, accept full responsibility for the task of furnishing to the consumers of the nation the products of our farms and factories; second, buy according to established grades and standards in order to make production subservient to consumption; and third, promote consumer education as to merchandise.[1]

1. *Retailers and wholesalers should accept full responsibility for the task of furnishing to the consumers of the nation the products of our farms and factories.*

Few retailers and wholesalers have any adequate conception of the economic significance of

[1] It is true that these suggestions only offer an indirect solution of the question stated in my second proposition. Transportation and land-tenure play tremendously important parts in the drama of distribution. But the question of the responsibility of our present railroad freight structure for the high cost of physical distribution would require a book of its own, just as the question of the responsibility for the high cost of distribution which may be attributable to our present system of land tenure would justify a volume exclusively devoted to that question. The railroad question and the land question have, however, been treated at great length and by many writers. The phase of the problem to which I have devoted myself has up to the present time been largely neglected.

the work they do. The men engaged in retailing and wholesaling have no consciousness of responsibility for distribution which is comparable to the medical profession's consciousness of responsibility for the health of the public. Yet there are reasons for their assuming that responsibility just as important to them and to the public, as there are reasons for the assumption by physicians of responsibility for the public's health.

Today there are two different methods and conceptions of the work of retailing and wholesaling in irrepressible conflict.

By one of the conceptions, the manufacturer is supposed to take full responsibility for the distribution of the products he makes. He is supposed to identify his product, create a demand among consumers for his brand with national advertising, and use wholesalers and retailers merely as agents for distributing his products to customers who have been "sold" by the manufacturer's advertising. The retailer is supposed to be the agent of the manufacturer and the retail store is supposed to function like a slot machine. The retailer is supposed to stock goods in accordance with the demands of his customers for the various brands. He is not supposed to influence his customers to buy merchandise which he selects because in his judgment it meets in price, quality and style the needs of the trade to which he caters. The retail store is supposed to be merely a convenient place in which it is possible to get the

particular brand which the customer has been persuaded to ask for by the manufacturer.

By the other method and conception of the retailer's work, the retailer is supposed to act as the purchasing agent for the community he serves. Out of the offerings of all the manufacturers, the retailer is supposed to select those which from the standpoint of quality and price and style will best satisfy the wants of his trade. If his selections are well made, he will have little difficulty in convincing his customers that his judgment was sound and that they should be guided by his experience.

The first of these two methods requires high-pressure marketing by the manufacturer, and results in shifting the burden of leadership in distribution from the distributor to the manufacturer.

Day by day, the direction of distribution becomes more and more the work of manufacturers. They determine arbitrarily how products shall be marketed and through what channels they shall be distributed. Manufacturers create channels of distribution to suit themselves and adopt marketing plans quite without regard to the effect of their plans upon the cost of distribution generally. Each manufacturer seeks to persuade the wholesaler and retailer to stock his brand quite without regard to the fact that the abandonment of existing brands by a distributor or the addition of unnecessary new brands, (if the exist-

ing ones are retained), lowers turnover and raises costs by unnecessarily increasing stocks.

If the retailers and wholesalers of the country continue in increasing numbers their acceptance of the place in the scheme of distribution to which these tendencies consign them; if they permit the manufacturers to direct more and more of the work of distribution, then it is only natural that they should receive less and less for the work that they do; that manufacturers should constantly shrink the margin upon which distributors work, and that the total cost of distribution—the combined cost of distribution of both manufacturers and distributors—will cost consumers more and more.

To remedy this state of affairs, retailers and wholesalers must assume the responsibilities of their position in our economic system. They must force the manufacturers of the country to recognize that retailers are better interpreters of the needs of the public than the manufacturers and that manufacturers must distribute their products through those channels of distribution which in the long run are most efficient and economical.

Self interest and public interest both dictate that retailers and wholesalers should perform a selective service for their customers and not an automatic service as distributing agents for the manufacturers.

Retailers and wholesalers should therefore fit themselves to intelligently supply the wants of

their customers—to perform the work they have chosen to engage in efficiently and economically. To do this, they must actually make themselves responsible for distribution—individually and as an organized body. The economic function which wholesalers and retailers perform is a vital part of the work of distribution. They must assume the direction of that work if they are to properly serve the public and to deserve and receive an adequate return for the work they do and the capital they invest in their businesses.

2. *Retailers and wholesalers should buy according to established grades and standards in order to make production subservient to consumption.*

Today the numbers of products purchased by wholesalers and retailers in accordance with recognized grades and standards are few and far between. The retailers' capacity for judging merchandise has been almost entirely destroyed by the widespread habit of buying by brand instead of in accordance with established grades. Yet no other thing would so greatly help in reducing distribution costs; first, by reducing national advertising, eliminating high pressure marketing, and doing away with the confusion of fictitious selling and advertising points; secondly, by reducing the variety of brands retailers and wholesalers would have to carry, thus speeding turnover and reducing mark-downs; and thirdly, by lowering manufacturer's marketing costs, reduce prices, thus

making it possible for a greater number of consumers to purchase the product, or for existing consumers of it to purchase the product either in larger quantities or of better qualities than before.

That retailers and wholesalers can well afford to represent the interests of their customers by buying this way, and by promoting standardization, is to understate the situation. They can not only afford to do it without loss, but they can afford to do it because it will add to their own profits.

A grocer located in a section in which consumers earn an average income which enables them to spend $10 per week with him, will sell $10 worth of groceries to each of his customers. From week to week and season to season, the grocer's stock may change. He may sell bulk coffee at low prices per pound or package coffee at higher prices. He may sell cereals as nature made them, or he may sell them transformed into breakfast foods. But in all cases, he will find that his sales to his customers will still average $10 per week per customer. Nothing will change that except a change in his customers' income.

If he sells coffee, cereals, sugar, and canned goods by grade instead of in advertised packages, he will be able to give his customers either more for their money in quantity, or more for it in quality. That ought to be a sufficient incentive to make him really strive to act as their purchasing agent. But if that is insufficient, the fact that he

can secure a better margin of profit on the goods which he thus selects for his customers ought to make him anxious to re-orient his buying, his selling, and the arrangement of his stock so as to make this method of operating profitable, economic and hygienic.

What would follow from this is well set forth in the following extract from an article by Stuart Chase and F. J. Schlink:[2]

When goods are bought to specification, quality is set; scientifically defined. The buyer knows exactly what he is getting; the manufacturer knows exactly what he has to produce. Competition must then descend from the cloudy heights of sales appeals and braggadocio generally, to just one factor—price. Who can meet the specification at the lowest price? Quality being predetermined, there is no longer any argument as to who furnishes the "best" product—there isn't any best or worst to furnish except as the product may be better than the required minimum for the grade in question. And down the trapdoor goes all the advertising and all the salesmanship which falls under the general head of persuasion—to use no harsher terms. Down goes the distribution overhead, and with it the cost of the delivered article.

Secondly, when competition is on price only, a battering ram begins to operate on profit margins. The manufacturer who shades his profit per unit the most, is likely to get the order. Down goes the cost to the consumer again—the maker secures large distribution at a

[2] *The New Republic,* December 30, 1925, pp. 154-155.

small margin of profit per unit—the Ford-Filene idea. Both manufacturer and consumer benefit.

Thirdly, the manufacturing process itself tends to become simplified. It is no longer necessary to make so many styles and variations on the chance of catching the consumer's eye. "Special features," fancy packages, drop out of the picture. One can produce in large units; one has a better chance of "balancing the load" in plant operation. Thus the concern which now makes the government's ink has divested itself of all snappy executives and expensive trappings, and in a plain but well lighted loft in downtown New York, bends all its energies to making good ink, day in day out, with no fear of seasonal variations, fluctuations, or market upsets during the present contract. Less romance, perhaps, but more sound workmanship. With the drop in manufacturing costs, down goes the price again.

Fourthly—and this is a category of the utmost importance—the consumer, buying to specification, is in a position to buy for a *specific purpose*. If tests have made it clear that a cheaper product or a lower grade or a different product will adequately meet his need, he can buy the cheaper article and save the difference. *He no longer has to protect himself by paying the highest price, fearing that cheaper grades will be adulterated, or go wrong.* How often have you and I paid through the nose because our only test of quality was the highest price in sight. For certain uses, the Society of Automobile Engineers reported that lubricating oil costing twenty cents a gallon was as good as oil at $1.35. It met the specifications, and the purpose, at one-seventh the cost. Tests show that certain hardware in ten-cent stores has just as good steel as hardware in stores where

the price is two or three times as much. The latter article has a little fancier handle, but for a given use, the tools are identical. Government research finds that for many uses reworked wool has better wearing qualities than all-virgin wool. It finds that certain limestones make better building material for specific uses than sandstones—thus upsetting an ancient dogma. If and when the consumer can be guaranteed by test and specification that the cheaper grade meets his purpose as well or better, down goes the price again.

Fifthly, buying to specification eliminates all possibility of deliberate adulteration. It drives the specious, the jerry-built, the actively hurtful from the market. Such products often represent a dead loss of manpower and raw material in the making, to say nothing of the terrific overhead burden of astute salesmanship which now keeps them on the market. In the aggregate this too will operate to lower prices by eliminating waste.

Let retailers and wholesalers once begin to buy in this way, and we shall see with amazing rapidity that production will become subservient to consumption and that the consumer's best interest, rather than the manufacturer's best interest, will be served by the marketing methods of our manufacturers.

3. *Retailers and wholesalers should promote consumer education as to merchandise.* To bring about the transformation in buying outlined above, it will obviously be necessary to re-educate consumers. They will have to be taught to buy by grades instead of by brands. They will have

to be taught to look to the Bureau of Standards in Washington for information about what to buy instead of the advertising section of their favorite magazine.

The practicality of this is apparent from the following in the article by Stuart Chase and F. J. Schlink,[3] from which I have already quoted:

> Each year the government buys some $300,000,000 of products—ranging all the way from thumbtacks to dredging machines; from baseballs to battleships. Nearly every kind of thing the general consumer buys, the government buys—though in not such great quantity—foodstuffs, textiles, clothing, furniture, building materials, office supplies, shaving tackle, sporting goods, toilet articles . . . everything. But in buying much of this material, the several purchasing agents pay no attention to pretty girls or magazine covers, nor yet to super-salesmen with pants like the Prince of Wales. They pay attention to instructions from the Bureau of Standards. Half-way between Washington City and Chevy Chase, these great laboratories and testing rooms rise—magnificently on guard. Skilled chemists, physicists, engineers, research workers, in a hundred fields are passing continually and relentlessly upon the relative quality of the goods which the purchasing agent proposes to buy. During the last fiscal year, the Bureau made no less than 173,000 tests.
>
> The government alone has developed over 11,000 specifications covering, besides foodstuffs, soaps, denims, metal polishes, hooks and eyes, motor boat engines, shipping cases, and so on indefinitely. The total of specifi-

[3] *The New Republic,* December 30, 1925, pp. 153-154.

cations available from all sources runs to something like 27,000.

Here are two simple government specifications covering the purchase of foodstuffs:

Chocolate—best quality unsweetened: to contain not more than 3 per cent of ash insoluble in water, 3.5 per cent of crude fiber, 9 per cent of cocoa starch, and not less than 45 per cent of cocoa fat per pound. (Such chocolate the government buys for 15.5 cents a pound. We pay around 45 cents, retail distribution costs included.)

Gelatin—granulated in packages: must not contain bacteria in excess of 50,000 per gram, arsenic in excess of 1.4 parts per million, copper in excess of 30 parts per million, and zinc in excess of 100 parts per million.

Unless consumer education as to merchandise is to be a mere pious desideratum, it is necessary to determine whether any instrumentalities for consumer education exist, and if so, whether the available instrumentalities are sufficiently independent of the national advertisers to undertake the task.

Innumerable instrumentalities for consumer education do exist. The schools, women's clubs, labor unions, and farmers' organizations are typical of them. Unfortunately the instrumentality for consumer education which is most important —the newspaper and periodical press—cannot afford to undertake the task. Periodicals are supported either in their entirety or in large part by the national advertising of manufacturers. Instead of educating consumers and teaching them

how to discriminate in buying, it is in the interest of the national advertisers that the publications try to blunt the consumer's sense of values. What is worse, since education, and club life, in fact the whole of society in America, takes its tone so largely from newspapers and magazines, important avenues of possible consumer education are unaware of the need of this education and are deprived of the facts upon which it must be based.

One instrumentality does, however, exist which can afford to educate the consumer. That is the retail store itself. And here, fortunately, the education of the consumer can be carried on most effectively. Instead of mechanically handing out the various brands for which consumers ask from day to day, the retailer and his sales clerks can educate them most effectively in the very act of selling them the merchandise which he has in stock and which he has selected as the best in price, quality, and style. In doing so, the retailer will win the respect of his customers, build goodwill for himself, and earn the greater profits which will inevitably come to him.

XIX

CAVEAT EMPTOR!

Buying is a neglected art.

Yet distribution is regulated at every step by buying.

Distribution begins when an elevator *buys* a farmer's wheat. It proceeds when the flour mill *buys* the wheat from the elevator. It continues when the wholesaler *buys* from the miller, when the retailer *buys* from the wholesaler, and it ends when the ultimate consumer *buys* from the retailer.

There is no adequate appreciation of the significance of this fact.

The discussion of buying in our rather extensive literature of business is singularly meager. It is as meager as the treatment of selling is bounteous. As a nation we seem to have dedicated all our energies to selling and all our "best minds" to the solution of problems of salesmanship. The important part which buying plays in distribution has been overlooked probably because economy in buying seems a "negative" rather than an "affirmative" virtue. We seem to have quite overlooked the fact that every act of selling is accom-

panied and indeed is conditioned upon an act of buying. What is most unfortunate, preoccupation with the art and science of selling seems to have actually resulted in the atrophy of the art and science of buying.

Yet buying is far and away the more important.

A little consideration of the part played by buying in our economy will show, first, that buying regulates all distribution; second, that extravagances in marketing cannot be passed on to buyers unless buyers are ignorant of commodity standards or market values; third, that consumers generally are entirely without knowledge of merchandise values; that buying for resale is automatic rather than selective, and that only in the case of buying for industrial use are buyers even to a limited extent technically qualified to determine the value of the things which they buy.

This is a state of affairs that points clearly to the need of a real study of the subject of buying.

It is true that some studies of buying have been made which deal with the practical problems of the buyer and purchasing agent, but so little has been written concerning the economic aspects of buying as to make this phase of the subject virtually unexplored territory. I have, therefore, ventured upon an outline of certain salient aspects of the economics of buying, and trust that others may be inspired to undertake a complete exposition of the principles involved.

Buying may be classified as, first, the buying

of raw materials, parts, and supplies for re-fabrication; second, the buying of finished and unfinished commodities for re-selling; and third, the buying of finished commodities for ultimate consumption.

BUYING FOR RE-FABRICATION

Nearly all our raw materials and semi-finished products are bought for re-processing—for fabrication into finished products. All our industrial buying, including the buying of fuel and power, machinery, and supplies, is incidental to the re-fabrication of raw materials. The mill which spins and weaves cotton into cloth, not only buys raw cotton, but it buys spindles and looms, coal for its power plant, oil for lubrication, and a thousand other products all of which directly and indirectly are used in the fabrication of cotton goods.

What is the principle which governs the buying of commodities for re-fabrication? In what does it differ from the principle which governs other kinds of buying? We must answer these questions if we are to come to an understanding of the part which buying should play in the solution of the problem of distribution.

In the spinning of the yarn and the weaving of the fabric, for which practically the entire cotton crop is used, certain definite qualities or characteristics of cotton are selected by the mill-buyer because these qualities are essential in the manu-

facture of the kind of goods which this mill produces.

It is not enough for the buyer to know that the cotton he is considering buying is priced correctly —he must know the color, luster, and brightness of the lint; the nature and amount of foreign matter present in the lint, such as leaf or dust; the preparation or ginning, and the length of its fibers.

What is true of cotton is true of pretty nearly all the commodities which are purchased for reprocessing for industrial use. In buying for this purpose, the purchasing agent pays little attention to extraneous matters like pretty advertisements or high-powered salesmen and concentrates upon the qualities of the product which he is buying.

In buying for refabrication, the principal question is whether the product conforms to the standards or specifications established for the work in hand. This fact having been established, the question of price becomes very largely a matter of agreement between buyer and seller as to just what actually is the current market price.

BUYING FOR RESELLING

Two great groups of middlemen, one group operating in raw materials and the other in finished products, are engaged in buying for reselling.

The first of these two groups are the merchants who buy, assemble, grade, and resell raw materials and semi-finished products.

When cotton is sold by the actual grower of the fiber, it is first bought by a local storekeeper, factor, or agent. From these local factors it is bought by the cotton merchants. Both the local factor and the cotton merchant, one of whom may be said to be a retail assembler of raw cotton and the other a wholesale assembler, buy purely to resell. The only change which the cotton undergoes while passing through their hands is that of grading and assemblage. The consideration which governs them in their buying therefore is solely one of making certain that the intrinsic quality of each lot of cotton is accurately reflected in the price they pay. In buying, therefore, the two considerations which are never for the moment lost sight of are those of grade and price.

The second group of buyers for resale are the wholesalers and retailers who buy finished commodities for distribution to the ultimate consumer. In this group the consideration which governs buying today is altogether different.

Fifty years ago the buying of finished commodities by retailers and wholesalers was governed by precisely the same principles relating to grade and price which prevail today in the buying of raw materials. The development of brand specification and the gradual destruction of all the established grades and standards with regard to finished products has almost universally destroyed wholesalers' and retailers' abilities to function selectively in buying.

As long as cotton sheets are purchased by the wholesaler and retailer on the basis of grade and price—as long as the count of warp and filling, the fineness of the yarn, and the quality of the finishing are considered in connection with price, the buyer for wholesaling and for retailing both perform a selective function with regard to all the merchandise which passes through their hands. As soon, however, as the sheeting ceases to sell on its intrinsic qualities, but purely upon the demand for a certain brand, the wholesaler and retailer cease to exercise any selective function in buying it. It is obvious that the greater the extent to which brand specification enters into the buying by the ultimate consumer, the less will the retailer and wholesaler perform a selective function in buying. Yet this selective buying is absolutely essential if manufacturers are to be prevented from charging more than competitive prices for their products.

To make this clear it is worth while considering the full significance of a true competitive price. A true competitive price can only be established in a competitive market. An excellent statement [1] of the attributes of a competitive market is made by Edmund Brown, Jr.:

(1) A common meeting place.—For a market to be open and competitive it must be possible for buyers and sellers to meet and trade. This does not require that

[1] "Marketing," by Edmund Brown, Jr., pp. 6 and 7.

they meet on a trading floor or in a particular market space: it means that by using the facilities at hand—telephone, telegraph, or a trading floor—any reputable buyer should be able to trade with any reputable seller, and vice versa, without artificial hindrance.

(2) Common knowledge of market information.—Buyers and sellers must have convenient access to all facts as to who the other buyers and sellers are, the potential supply and the potential demand, and the price established by previous transactions—i.e., a common knowledge of the general conditions under which they operate.

(3) Indifference to identity of product.—In such a market the commodity offered by any seller at a market price will be identical in physical character and quality with the commodity offered by any other seller at a market price, so that it is a matter of indifference to any purchaser whether he buys from one seller or another. The commodity, therefore, must be standardized. All sellers must be willing to sell to all buyers on equal terms. This indifference must function freely and every buyer and seller in the market must be able to take advantage of the market price, so that no buyer and no seller can be forced by individual necessities to depart from that price.

It is very obvious that the absence of any one of these three elements destroys a true competitive market and makes it impossible then to establish a true competitive price. In the buying of raw materials for resale true competitive markets are generally prevalent, but in the buying of finished products, the prevalence of brand specification has

all but destroyed the normal basis upon which true competitive prices can be established. If we are to eliminate high pressure marketing, it is perfectly plain that we must re-establish the buying of finished products for sale to the ultimate consumer upon a basis of the intrinsic qualities of the goods and put branding in its proper place as subsidiary to the merchandise itself. Upon this point let me quote Mr. Saunders Norvell:[2]

Once upon a time, the retail drug merchant was an authority in his community on drugs and chemicals just as today the hardware man is an authority on axes, hatchets, and saws. When a man wished drugs and chemicals he went to his friend, the retail drug merchant, and asked his suggestions and advice in regard to the kind and the quality of goods to purchase. He was guided by this advice.

This condition, while it still exists in the hardware trade, has entirely passed away in the drug trade. Nowadays the national advertiser in the drug business thinks up some highsounding name, advertises his goods nationally, on one hand frightening the consumer about the condition of his health, describing his symptoms, and on the other hand, promising him a cure or relief if he will only buy his concoction. Then in his advertising he warns everybody against substitution. If any retail drug merchant would have the temerity to say to a customer, for instance—"This other preparation made by me is 'just as good' "—that drug merchant would

[2] Chairman of the Board of Directors of McKesson & Robbins, Inc., New York, manufacturing druggists. Reported in the *Hardware Retailer*, November, 1923.

immediately be classified by the intended purchaser as a fraud and a cheat.

What is the result?

The retail drug merchant today knows nothing whatever about salesmanship. He does not try to sell goods. His clerks, like automatons, stand behind the counter and pass out the goods that are called for—that are nationally advertised. They have nothing to say about these goods. They would not dare to make any suggestions. They take the money, punch the cash register and turn like a machine to repeat the same performance with the next customer that national advertising has driven into their shops.

Now what has brought about this condition? The answer is simple—national advertising. The manufacturers of a long line of drugs and toilet articles have bought space in newspapers, magazines, on street cars and on billboards, and have proceeded to sell their goods to the public. The greatest of these manufacturers openly boast that they do not ask any selling ability on the part of drug jobbers or retail merchants. All they ask is that their goods be carried in stock and that orders be filled when the goods are called for. This all seems very simple and delightful, but when we analyze the profits that the jobbers and the retailers are making on these nationally advertised goods, we soon find that the goods are being sold, by reason of competition, at less than the actual cost of handling the business.

Today the retail hardware man, thank God, is still an authority on hardware in his own town. If a man wishes to build a house he goes to him and asks his advice in regard to builders' hardware. If a man wishes to buy a set of tools, he goes to his retail hardware

friend to help him make the selection. If the time ever comes when builders' hardware, tools, and other articles in the hardware line are advertised as they are in the drug line, this condition will entirely pass away. When a man goes to buy his builders' hardware or his tools he will know, or he will think he knows, exactly what he wants, and woe to the retail hardware merchant who would dare to suggest to him what he should buy! If he does, this retail merchant will be branded as a "substituter," and the consumer will go to some other store where he can get what he wants without trying to have any other brand put over on him.

Therefore, while no one believes more than I do in certain kinds of advertising, let me utter a warning against this chimera of national advertising. In the end it will be a bad thing for manufacturers, jobbers, and retail merchants, just as today it has almost completely demoralized and ruined the wholesale and retail drug business of the country.

BUYING FOR ULTIMATE CONSUMPTION

When we come to the practices which today prevail in buying for ultimate consumption, we find that less than one hundred years of divorce between production and consumption has almost entirely destroyed the consumer's capacity for measuring quality.

Up to the beginning of the industrial revolution over one hundred years ago, the ultimate consumer was a self-sufficient animal. He produced for himself most of the things which he consumed.

Those he could not produce himself, he secured directly from craftsmen who could make them for him. Products which are now factory made were home made or custom made.

In determining the value of the things bought, the consumer of that time had the tremendous advantage of observing all the processes involved in their production. Thus he was able to familiarize himself with the factors which determined the value of what he bought. He met the maker of the products he bought on common ground with a common understanding of what constituted value. These conditions made him an infinitely shrewder buyer than is the consumer of today. Even the least observing man of that day knew more about the production of the things he bought than the most observing consumer of today. The consumer of the days previous to factory-production knew about foodstuffs because practically everything that he ate was grown, often on his own farm, and milled right within his own neighborhood. He knew about the textiles he used because he raised his own wool and flax, saw the yarns spun and woven, if not in his own home, certainly on looms the operation of which he had witnessed until he was sufficiently familiar with weaving to judge intelligently the qualities of the fabrics. When he ordered hardware and furniture from his local blacksmith and cabinet maker, he was sufficiently familiar with the making of the things he wanted

to specify the materials to be used and the methods of workmanship to be employed.

It was just as easy then as it is today to fool the consumer about merchandise with which he was unfamiliar, but it was impossible to fool him then, as it is possible to fool him today, about the value of the commodities which he bought day after day and year after year.

Today the consumer, when in the market, is confronted with a factory made product, the qualities of which are influenced by his needs and desires only in the most indirect fashion. Factory production of necessity results in a divorce between production and consumption. Through this change the consumer is confronted with a problem in buying the significance of which we scarcely appreciate.

The consumer of today has little opportunity to learn about the raw materials which enter into the products he buys, or the methods used in fabricating them. The very abundance of the times has confused him, disarmed him, and tended to make him the helpless and credulous victim of the manufacturer's propaganda. Let him be deprived of the guidance of the independent retailers, who select merchandise carefully because the retailers' survival is dependent upon intelligent selection, and he will be entirely helpless.

In buying today the consumer is therefore credulous and gullible. He is influenced by arguments pitched in a key to appeal to intelligences whose

average is no higher than those of eleven and twelve year old children.

"The American buying public," said a very successful business man who is a shrewd student of marketing methods, "consists of one hundred million morons."

An advertiser of one of New York City's largest department stores quotes an English poet who said, "Nowadays, people know the price of everything and the value of nothing."[3]

Today the consumer is reduced to a state in which he has no other method of judging the relative value of two products than by the prices which are asked for them. If the price of one is higher than the other, he assumes that the higher priced one must be superior. He knows too little about the factors involved in producing the product itself to determine whether or not the higher priced product really represents a commensurate increase in value. And yet he flatters himself that he is so much wiser than his forefathers!

Under such conditions it is no exaggeration to say that the consumer has surrendered the satisfaction of his needs and desires to the direction of high pressure salesmanship and to high pressure advertising. It is because these modern agencies for his guidance are failing to furnish him with goods at the lowest cost which modern methods and inventions make possible, that we are confronted with the necessity of establishing dis-

[3] James A. Hearn & Son, New York.

tribution practices which will once again make production subordinate to consumption.

So accustomed are manufacturers who are engaged in high pressure marketing to the discussion of the problem of distribution from the point of view of the producers only, that any effort to make them realize that after all production exists for the benefit of the consumers and not consumers for the benefit of production will come to them as an intellectual shock.

There are three principles which these manufacturers must accept if they are to reconcile themselves to the principles of buying here enunciated.

(1) That consumers are entitled to secure the goods needed and desired by them at the lowest possible cost; (2) That it is in the general interest of the community as a whole—the interest of the consumers and producers taken together—that distribution and production be economically conducted; (3) That whenever any factor in the process of distribution, i.e., any retailer, wholesaler, or manufacturer, aggrandizes himself by methods which tend to increase the cost of distribution, such methods are not justified by sole virtue of the fact that the man who employs them finds them profitable.

No business exists entirely to itself.

No business man has the economic right to profit by sacrificing the general welfare to his individual profit.

Most of the ills and ailments of distribution may be traced to the failure to bear these principles in mind in buying—the basic regulating device in our process of distribution. The extravagant marketing methods which exist today are those which individual manufacturers have found most profitable to them. The general welfare has suffered from what might be called a state of anarchy in distribution—of unrestrained license upon the part of manufacturers.

The check upon the manufacturer represented by informed buyers no longer exists. The ultimate consumer knows little or nothing about the intrinsic qualities of the merchandise he buys from the retailer. And the retailer follows the path of least resistance, and hands out to the consumer only those products which the enterprise of manufacturers makes it easy for him to sell.

If the disappearance of the informed buyer has produced these extravagances of distribution, then it is obvious that the re-appearance of the informed buyer would result in their elimination.

If any appreciable number of consumers were to begin buying to the tune of an old Latin saw, "Caveat Emptor," high pressure marketing could not survive.

The theory upon which consumers have been persuaded to abandon *caveat emptor* is in substance this—the manufacturer assumes the risk of satisfying the consumer, and the consumer need not therefore examine carefully the article he is

buying, because he can rely upon the manufacturer's guarantee rather than upon his own judgment or that of the retail dealer.

In effect, the consumer is made to feel that it is unnecessary for him to have any technical knowledge of the product which he buys because, if he confines his buying to well known brands, the self-interest of the manufacturer will prevent him from selling merchandise which might endanger the consumer's goodwill. The manufacturer will, presumably, be too intelligent to make shoddy goods in order to earn a slightly larger profit, if that is apt to endanger the consumer's continued preference for the manufacturer's brand.

There is no question about the fact that this shifting of responsibility has introduced a pleasanter atmosphere into the relations of consumers and manufacturers, at least superficially. It is extremely doubtful, however, whether even this superficial improvement offsets the great disadvantages which have followed upon the sacrifice of the buyer's independent judgment in this fashion. With the manufacturer no longer forced to meet the critical judgment of the consumer, it is perfectly natural for the manufacturer to develop methods of marketing which will yield him the highest net profit, regardless of the intrinsic value of his product.

What is needed, therefore, is a skeptical and critical attitude toward merchandise—an attitude

which in these days is somewhat out of fashion.

Whenever an article is offered the consumer in such a form as to make it difficult to intelligently determine its value—when it is packaged, or branded, or he finds himself importuned to buy it by any of the devices of high pressure marketing—what he needs to do is to act on the principle of *caveat emptor*—let the buyer beware.

The extravagances of high pressure marketing cannot survive general practice by the public of the principle of *not buying high priced goods whenever it is possible to buy equally as good products for less money.*

XX

HOW MUCH IS A PACKAGE?

If we take a little time to reflect we cannot fail to be profoundly impressed by the sweeping changes that have been made in our buying habits during a single generation. When we take an inventory of the things we are compelled to purchase for the maintenance of life as it is lived today, we realize how completely we have become surrounded by packaged products. It requires real ingenuity to buy many of the things in the form in which we were accustomed in childhood. Instead of going to the bakery, and getting a bag of fresh-cooked crackers, direct from the oven, hot to the touch, and delicious to the palate, we must be content with a carton of biscuits half the weight of our early day bag, and less than half the quality, at two or three times the price. In this, as in many other cases, modern methods of marketing have increased the cost and diminished the quality of living.

It is true that the grocery of some twenty years ago, with its unsightly sugar barrels and cracker boxes, its dried fruit bins, and its long rows of tea, coffee, starch, rice, and other cereal boxes,

and its inappreciation of the fact that foodstuffs were intended for internal consumption, has not a particularly savory place in our memories.

Things are today, at least with regard to the handling of food, better than they were. The unforgettable "Jungle" of Upton Sinclair, the pure food campaigns of Dr. Wiley and Alfred McCann, and the evolution of the old ideals of good-cookery and cleanliness into the sciences of dietetics and hygiene, have changed this indifference of most people into demands for ever higher standards of cleanliness in food. Methods of distributing food which were accepted without question a generation ago would not be tolerated today.

It is true that the idea of the sanitary packing of food in convenient cans and cartons at the factory was one of the most important influences in bringing about this change. Twenty years ago, ninety-five per cent of the dry groceries were sold in bulk; to-day, seventy-five per cent reach the consumer in package form. It is merely justice to accord to the advocates of the package idea the credit for introducing a valuable improvement in our methods of handling groceries. But it is foolish to overlook the fact that their motive in introducing packages was the desire to add to their profits by making it easy to advertise their goods and to manipulate the prices which they receive for the product itself by arbitrarily determining how much they place in each package.

Just as today's grocery has become, as a result

of these influences, an entirely different institution from that of yesterday, so is the modern kitchen entirely different from the kitchen of fifty years ago. The package has wrought great changes in the American pantry. Today's housewife buys a small package, of a size that is carefully designed to send her frequently to the store to replenish her supply, tightly sealed and packed with clock-like precision by automatic machines, with the quantity in each package guaranteed not to vary over a sixteenth of an ounce, and its standard of quality backed, no longer by the reputation of the merchant, but by the national advertising of the manufacturer.

The kitchen of today, especially in the cities, is more compact. The elevator made the skyscraper possible; the package has made the kitchenette home possible. The modern kitchen contains a greater variety of foods, and its care is much less laborious than the kitchen of years ago. But it is incredibly more extravagant. In spite of these conveniences of which we boast as products of a superior civilization, the home does not turn out anything like the volume of food, laundry and sewing which the housewife of former years turned out as a matter of course. For the privilege of buying in packages and bottles instead of in sacks and jugs, and for buying its jams and jellies and fruits and vegetables in tin cans containing whatever the packers in the generosity of their hearts choose to embalm in them, the house-

wife has very largely abandoned the preserving of all these foods in the good old glass jar. If this is progress, then I am for the reaction. To can your own fruits and vegetables, improving upon your forbears only by using the inventions of modern science in preserving under steam pressure and in using materials and appliances which lessen the labor involved, pays not only in dollars and cents, but physically and gastronomically.

The package idea is good, especially with foodstuffs. It deserves reasoned support, but because it is a clean and convenient method of handling foodstuffs, consumers should not permit it to be a means by which their pockets are deftly picked of pennies and nickels and dimes which, in the aggregate, represent a very considerable share of their total expenditures.

It is more economical to buy in bulk from the most expensive grocery stores in New York City, than to buy in advertised packages at the corner grocery.

Packed, as are so many advertised articles, in bulky cartons, in panel bottles that are tall and thin, in pretty little jars and glasses, the manufacturer has discovered a way to eat his cake and save it too. He takes credit for selling either a "big" or a "convenient" measure; he actually gives less than the quantity which his customers were previously in the habit of buying.

Some years ago the Commissioner of Weights and Measures of New York started a movement

which spread all over the nation. He urged the people to watch for the manipulation of scales and measures by tradesmen who did not scruple to stoop to petty thievery. In New York he succeeded in having hundreds of tradesmen and peddlers fined, their scales and measures condemned and confiscated, and their businesses injured by the publicity which followed the exposure of their roguery. The butcher, who stuck a piece of tallow weighing an ounce under the pan of his scales and cheated his customers to the extent of one ounce on their purchases, was exposed, haled to court, fined, and reprimanded severely.

There is a distinction, but no real difference, between this butcher and the manufacturer who packs his product in a "pound" package which weighs fifteen ounces. The motive which animates both is the same; the desire to add to their profits by giving the customer a trifle less weight than the customer is willing to pay for. The manufacturer, however, picks pockets with a better knowledge of the law. He does openly and brazenly what the other does secretly. With a hypocritical pretense of absolute honesty and his unctuous claim that the measure is accurate to the fraction of an ounce, the advertiser prints the net weight packed in his package somewhere about the package. He complies with the law in as small a type as possible. You generally have to hunt on the label of packages you buy for the net weight, but you can usually find it if you are curious enough

and do not mind an occasional strain upon your eyes.

The package, which ought to be primarily a means for conveniently and hygienically handling foods, and only incidentally a means for attractively displaying itself on the shelves of the retail store, has been used by many manufacturers principally for the purpose of craftily raising the price of their products to the consumer. By reducing the quantity in the package and maintaining the original price, the price is raised without the consumer being forewarned. By taking a package which originally weighed fourteen ounces and sold for ten cents and reducing it in weight to twelve ounces, it is raised in price one-seventh even if it continues to be sold for ten cents.

But the package may actually be reduced in price and still the price per pound increased. Take a package weighing fifteen ounces and selling for fifteen cents. Reduce the price to ten cents and the weight to eight ounces. The price of the package has been obviously reduced by one-third, but the price of the goods within the package actually has been increased by one-fifth.

The packages which fill the shelves and counters of stores today lend themselves to this kind of thing very readily. The products are rarely packed in standard units of measure. The package usually contains a little less than a half pound, a little less than a pound, or a little less than two pounds. It is easy for the public to think of it as

a half-pound, a pound, or a two-pound package. Five, six, or seven-ounce packages are handed the consumer when he asks for a half-pound; twelve, fourteen, or fifteen-ounce packages pass muster as pound-packages.

XXI

USELESS vs. USEFUL ADVERTISING

Modern national advertising is very different from the definition of advertising found in the dictionary: "To inform or apprise; to make known through the press."

This was the idea of advertising in the days when the merchant was content to print the fact of the receipt of a shipment of "New Orleans molasses" or of "Scotch ginghams."

"Such a conception of advertising," says Mr. George French in "Advertising," "is now not only inadequate, but false and misleading. It is now one of the minor functions of advertising to announce or give notice. *Its major function is to persuade.*" Mr. French is the leader of those advertising men who are engaged in the Herculean task of cleaning the Augean stables, and, to mix metaphors, of weaning the advertising world from the Fleshpots of Egypt. Moses and Aaron succeeded in weaning the Hebrews from the fleshpots of Egypt, but they had the assistance of Jehovah. Mr. French can look for no such divine interposition, and it is to be feared that without it he will serve as a convenient phraser of virtuous aspira-

tions which will merely cloak the old game of exploiting the credulity of the public.

Selling merchandise to the consumer by national advertising is selling merchandise in a very different way from that of the merchants of a less strenuous time. Then merchants used to assemble goods, and await the demands of the public. Both the makers and the storekeepers supplied the necessities of the public, but permitted the public itself to develop its own needs and propensities to purchase. Customers went to the stores because necessities, rather than artificially created desires, had developed in their lives. They bought goods when their pantry shelves were emptied or their clothes were worn out. The new things they bought were needed principally to replace those which had been consumed.

In a statement made before the Interstate and Foreign Commerce Committee of the House of Representatives, Mr. Edward A. Filene, of Wm. Filene's Sons Company, of Boston, gave a graphic picture of some of the evils caused by nationally advertised trademarked goods. Mr. Filene is an unquestioned authority upon merchandising. The company of which he is president is the largest specialty store of its kind in the world. Its annual sales exceed twenty-five million dollars.

All business men seek either to get out of the way of competition, or to get above competition. Getting above competition helps the public. That is, if we get above

competition by selling goods of the same quality at less price or a better quality of goods at the same price, we are performing a public service. We have no right to exist except as we serve the public, and fortunately, that we should not be tempted too much, we find as a general rule, that as we serve the public, so we flourish in business.

Mr. Filene then said that advertisers of trade-marked articles were not seeking to get above competition, but to get out of the way of competition, and that as more and more articles were trade-marked, finally almost all articles in common use would be sold out of the way of competition at prices higher than the cost of producing them warranted.

We ought not to do anything that will stand in the way of younger men growing up, with their newer and more up to the times ideas getting their chance. But they do not get their chance when the market is pre-empted by trade-marked articles, with the advantage of enormous profits and enormous funds to advertise back of them, so that by constant hammering of their names into the public mind, those articles get such possession of the buying public that reasoning buyers do not use ordinary reasoning and caution in purchasing them, and buy them because of their advertising, although they may have been reduced in quality or they may have been reduced in weight.

While all this is happening, and the old trade-marked thing is at least tending to deteriorate, there are being produced other articles—by young, more efficient, better

educated, better trained men—better for the public to buy in quality and design and in all things, and the public does not buy them because there have been such enormous profits in the trade-marked article that the public has been advertised and talked to and plied with booklets until they have come to believe that this article has superiorities that they, not being chemists and analysts and so forth, cannot find out that it does not possess.

In determining what advertising is useful and what useless to the consumer, there is no better criterion than Mr. Filene's. If any kind of advertising tends to increase price competition, and lower the price level of goods to the consumer, then that is useful advertising. If any kind of advertising tends to eliminate competition as to price or, as Mr. Filene puts it, to get out of the way of competition, then that advertising is, to put it mildly, useless.

National advertising, except when it is used to introduce new commodities, is a device for enabling a manufacturer to get out of the way of competition. It is, from the consumer's standpoint, a useless process of bragging. Retail advertising, on the other hand, generally intensifies price competition. The greater the amount of retail advertising in a city, the greater is the competition between the retailers. The public is offered better and better values by the retailers and prices are steadily reduced.

The retailer advertises for the purpose of in-

ducing people to trade at his store. To a great extent it is a matter of indifference to him just what they buy from him, so long as he has the opportunity of supplying their needs. His advertising is his method of notifying his patrons of his latest offerings. His real work is to assemble, literally from all over the world, attractive lines of merchandise at attractive prices, and whether his advertising pays him or not does not depend so much upon the persuasiveness of his advertisements as upon his merchandising skill. If he is to secure any permanent return from his advertising, he must continuously render a merchandising service that tends to reduce, little by little, the price of every article that he carries in his stock.

On the other hand, national advertisers are consciously and deliberately creating a demand for their trade-marked products for the purpose of capitalizing the good will which they create and then drawing additional profits upon this fictitiously evoked asset.

Mr. Paul E. Derrick[1] says of such manufacturers:

> They said to themselves, "There are so many million people who need exactly what I am making. They are every day buying something for exactly the same pur-

[1] "How to Reduce Selling Costs." As I shall have occasion to quote Mr. Derrick at length, it is worth while remembering that his authority and standing in the advertising profession is attested by the fact that he was the creator of the "Gold Dust Twins," the benign old gentleman so long associated with Quaker Oats, and the world famous character "Johnnie Walker."

pose as mine is intended. Some of the things are just as good as mine, some are not so good, and some are absolute rubbish. The public does not know whose goods it is buying and it does not care, but if it knew that it could not get anything better than mine, at an equal price, and if it could identify mine, and was entirely satisfied with them, I believe they would be asked for at the shops."

To market the goods, plans must be based upon efficient advertising to the consumer to interest him in the goods; to induce his initial purchase, and by the same means, to continue to stimulate his interest and purchase, and to create an atmosphere of individuality for the goods offered. He must be educated to think of "A's Biscuit," instead of biscuits; of "X Bread," instead of bread; of "B's Shoes," instead of shoes; of "Y Matches," instead of matches.

Mr. Derrick's description of the way in which national advertising enables manufacturers to reduce merchants to mere vending machines is illuminating. He is pleading with British manufacturers to follow the trail blazed by the national advertisers in this country, and for that reason describes the entire process in all its nakedness.

With the public "pulling" on the retailer for goods, as a result of the consumer advertising, it will require distinctly less "push" on the part of (the manufacturer's) salesman to secure a rapid and thorough distribution of them, and a constantly lessening effort and expense to keep them always accessible to the buying public. Indeed, by no other means can sufficiently

thorough and widespread distribution be effected to ensure the permanence of a large profitable business.

Salesmanship of advertised, price-protected lines differs essentially from salesmanship applied to unadvertised lines. The modern traveler is a representative of identified and advertised goods that represent the "house," not a representative of a remote and phantom house that his customer knows only as an address to which he makes occasional remittance. If qualified he is quick to appreciate the tremendous selling force which he controls when he takes out a well advertised line.

He finds the dealer more interested in the story of the advertising behind the goods than in mere discussion of the goods, or the price.

There are many opportunities offered the modern salesman to show the retailer how he can hitch his interests to the big advertising power with which the manufacturer is backing his goods. It is the salesman's business to demonstrate to the shopkeeper that it is to his interest to identify his shop with the advertised line, to attach the free advertising power to his business. . . . One of the economies of advertising is that it relieves the salesman from a great deal of the drudgery of selling. *He does not have continually to expound the value of the goods. Nor does he have to parry and thrust with his customers on the question of price.* He can at once enter into intimate relations with his customer. He should show him how to get the biggest possible part of the profit from the advertising which is being applied to the article. Thus relieved of spending his time in gaining the attention of the dealer, and bargaining and wrangling over prices and terms, etc.,

it is possible for the salesman to do his business with greater dispatch.

Is it not plain that by making it unnecessary for a retailer to discuss the quality, price, and value of the goods the salesman offers him, the national advertising of goods renders the retailer powerless to serve the interests of his customers? As a matter of fact, the salesman who sells an advertised product is seldom trained by the manufacturer to discuss these matters with retailers. He is a high pressure order taker. The merchant is compelled to buy from him. His customers have been persuaded by advertising to demand the advertised goods, and failure to supply them would merely result in his customers going to another dealer for them. Then, to induce the retailer to join in exploiting the consumer, he is shown by the salesman that what should interest him is not the true value which he might be able to offer his customers by careful inquiry into the nature of the goods and "bargaining and wrangling over prices and terms" so that he may be able to sell them to consumers at the lowest possible price, but the greater profit he can make on the advertised goods, either because of high gross profits, or because of the rapid turnover.

To cap the climax, Mr. Derrick says:

If the advertising is being efficiently done, and the salesman properly exploits it, the dealer, just the same as the consumer, has a conviction of the enhanced value

of the goods as compared with competitive lines, and the whole transaction of selling to the trade is to a great extent *lifted out of price competition.*

Mr. Derrick restates this argument in mathematical terms in two tables. He compares the division between the distributors and the manufacturer of the money received from the consumer for a cake of advertised soap and of unadvertised soap. In both cases, 100% represents the price which the consumer pays the retailer for the soap.

The Unadvertised Soap

Retail selling price		100%
Selling costs based upon retail selling price:		
Retail charge	33⅓%	
Wholesale charge	16⅔%	
Manufacturer's charge	5 %	
Total Selling Cost		55%
Balance of retail selling price in hand for expenses, production and manufacturer's profit..		45%

The Advertised Soap

Retail selling price		100%
Selling costs based upon retail selling price:		
Retail charge	25 %	
Wholesale charge	7½%	
Manufacturer's charge 5%		
Added for advertising 10%		
	15 %	
Total selling cost		47½%
Balance of retail selling price in hand for production and manufacturer's profit		52½%

These selling charges are exhibited throughout on the basis of the retail selling price, and, in the first example, based upon turn-over, are equivalent to 33⅓ per cent for the retailer, 25 per cent for the wholesaler, and 10 per cent for the manufacturer. In the latter

example, the selling charges are equivalent, upon turn-over, to 25 per cent for the retailer, 10 per cent for the wholesaler, and, including advertising, over 22 per cent for the manufacturer. We, however, find that we have still in hand 52½ per cent for production and manufacturer's profit as against 45 per cent for the unadvertised article—a positive saving of seven and a half per cent upon the total turn-over, figured on final retail price.

In other words, the economic advantage to the public is seven and a half per cent of its purchase price expressed in either better value, or lower price, or extra profit to the manufacturer. In any event it is increased national wealth due to increased economy and commercial efficiency.

It is almost incredible that a man of Mr. Derrick's experience in business should speak of this as of economic advantage to the public. That it is of no advantage to anyone but the manufacturers and the advertising industries is easy to demonstrate by giving this demonstration an "acid test."

Since Mr. Derrick has selected soap for purposes of illustration, we too will take soap for our counter-illustration. Instead, however, of comparing two hypothetical soaps, we will take two actual soaps, one of which is nationally advertised, and the other unadvertised. We will then be able to see what actually happens when the consumer's purchase price is divided between manufacturer, wholesaler, and retailer.

The nationally advertised soap which we shall use for comparison is a flaked soap—the most successful brand on the market. It is advertised as a special product to be used "For all fine laundering." It comes in a five ounce carton, and costs twelve cents.

The unadvertised soap is a similar product recommended "For delicate laundering," and costs twenty-two cents for a sixteen ounce carton.

The reputation of the advertised soap flakes is a reputation created by national advertising. The reputation of its unadvertised competitor is based upon the fact that it is sold with the recommendation of the grocery department of one of New York's largest department stores. There is no difference between the claims made for the two products. The directions for using them are identical. My own tests of the two indicate no discernible difference between them.

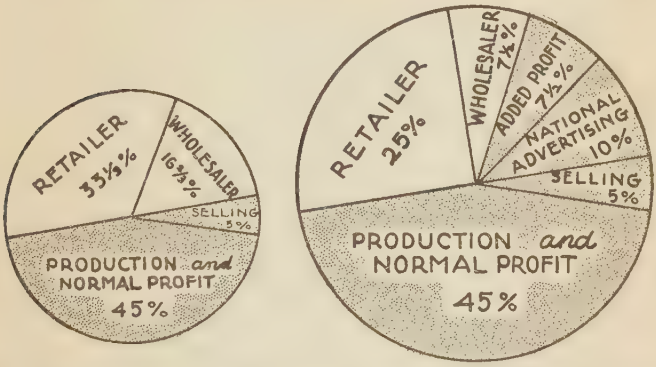
Now if both these two products are figured on the basis of 5 ounce cartons, and the consumer's expenditure divided in accordance with Mr. Derrick's formulas, this is how each factor in the sale would share in the consumer's money:

The Unadvertised Soap Flakes

Retail price of 5 ounces		$.06875
Selling costs based upon retail selling price:		
Retail charge (33⅓%)	$.02291⅔	
Wholesale charge (16⅔%)	.01145⅚	
Manufacturer's charge (5%)	.00343¾	
Total selling cost (55%)		.0378125
Balance of retail selling price in hand for production and manufacturer's profit (45%)		$.0309375

The Advertised Soap Flakes

Retail price of 5 ounces		$.12
Selling costs based upon retail price:		
Retail charge (25%)	$.03	
Wholesale charge (7½%)	.009	
Manufacturer's charge (5%)	$.006	
Added for advertising (10%)	.012	
	.018	
Total selling cost (47½%)		.057
Balance of retail selling price in hand for production and manufacturer's profit (52½%)		$.063



THE UNADVERTISED SOAP FLAKES THE ADVERTISED SOAP FLAKES

The two circles show the distribution of what the consumer pays for five ounces of the two soap flakes. The stippled areas show the amounts received by the manufacturer; the white areas, the amounts received by the wholesaler and retailer. Note how the shares of the wholesaler and retailer are reduced in order to make room for the national advertising and the added profit of the manufacturer of the advertised soap flakes, and how much larger is the sum paid by the consumer for the same quantity of advertised soap flakes.

These two tables show that every time the advertised article is bought by a consumer, he pays nearly twice as much for it as he would for the unadvertised article. He loses nearly 50 per cent

of what he pays; the retailer loses twenty-five per cent of his margin; the wholesaler loses on his margin forty-five per cent. But the manufacturer, after deducting marketing costs, (which instead of being less than on the unadvertised soap, as Mr. Derrick assumes, are nearly six times as much), *gets more than twice as much for his five ounces as does the manufacturer of the unadvertised article.*

Obviously, the manufacturer doesn't, as Mr. Derrick suggests, give the additional price which national advertising enables him to get to the public in a better value or a lower price.

He takes it out of the consumer's and retailer's and wholesaler's pocket-books and puts it into his own.

Isn't Mr. Derrick, to say the least, disingenious in describing the process of selling a nationally advertised product as an addition to the national wealth, when it is really a method of transferring wealth from the consumer, the retailer, and the wholesaler, to the manufacturer and the advertising industries which he supports? The consumer of an advertised article, it is plain, loses right and left, at every step in the movement of the goods from the manufacturer to his laundry, solely in order to contribute ten per cent of his expenditures to the support of the advertising industry and to enable manufacturers to double, treble, and quadruple their profits.

The greater the investment which the manufac-

turer makes in national advertising, the larger is the gross profit which he must make on his product in order to cover the expense of his advertising and the interest on his investment. If he increases his prices or reduces the quantity in his package, or lowers the cost of production, he is in position not only to meet heavy expeditures in advertising, but eventually to increase the amount which he can spend for this purpose. If, instead of spending $100,000.00 in creating and stimulating consumer demands for his goods, he spends $250,000.00, he is then in position to secure an even higher price for his goods and to increase his sales as well.

All national advertising tends to create vicious chains in which the increases in national advertising appropriations by manufacturers tend to increase the price level of all goods. As nationally advertised brands become more and more the dominant factors in any line of goods, the prices set by the manufacturers upon the nationally advertised goods become the market prices for all goods in the line, whether advertised or not. The unadvertised goods naturally profit by the situation. Instead of being normally priced at something above their cost of production, they are priced just below the price of the advertised goods. If nationally advertised canned soup sells at ten cents, and the unadvertised soups could be sold at a fair profit at five cents, instead of the unadvertised soups being sold at five cents, they

are naturally sold at just a little below the price asked for the dominant advertised soup, at nine cents. They are priced just a little lower than the nationally advertised line, but not nearly as low as they would be if the nationally advertised goods were not in existence at all.

Where is there in all this the slightest economy for those who consume nationally advertised products? If the manufacturer succeeds in his advertising campaign, he succeeds in increasing his individual profits. He succeeds in hypnotizing the public into asking for his goods irrespective of the price he sets upon them, and at the same time is enabled to demand from the distributors a larger share of the margin they would ordinarily receive from the public for the goods.

But the manufacturers are not content with the power which national advertising alone gives them in fixing the prices on their products. They have spent fortunes, both as individuals and banded in organizations, in trying to fix by law the prices at which retailers might resell to the public. So far as custom and advertising enabled them to do it, they always fix their prices. But what they are seeking by federal legislation to secure for themselves is the absolute power to reduce retailers to mere vending machines selling their products at uniform prices and at profits fixed by themselves. At one time it was the practice for them to try to do this by means of resale contracts, or by licenses based upon patents, but the courts held these con-

tracts and methods to be against public policy and to be violations of our anti-trust laws. At nearly every session of Congress for the past fifteen years they have tried to do it by securing special legislation, but Congress, for the same good reason, has refused to enact any law that would make the fixing of resale prices legal.

Unable to restrain price competition in this way, they have been driven to redouble the volume and the effectiveness of their advertising. Normal competition, competition in prices which tends to produce lower price levels, is thus more than ever replaced by advertising competition—competition in persuading the public that their brand is so much better than any competing product that the public will demand it in spite of high prices.

In addition to giving them power to raise consumer prices, it gives them the power to fix the profits which wholesalers and retailers who handle their products shall make. The greater the consumer pressure upon the dealer, the greater power has the manufacturer to reduce the discounts which he allows to his distributors, until on many advertised articles the distributors do not make enough to cover their operating expenses.

As Mr. Edward A. Filene puts it in the statement from which we have already quoted:

> I have been through it and suffered from trade-marked articles that I had to sell at less than cost. I had to buy and sell at a price that did not leave a living profit.

What happened with trade-marked goods, which at first we were induced to handle because of a reasonable profit, was that the retail price became fixed by advertising and custom. You could not increase it, because if you increased it, the customers thought all your goods were subject to the same increase, which was not true. But the price to us was increased by the manufacturer until there was not a living profit in distributing the goods.

You can get a great many instances of that kind of thing. The tendency is with many trade-marked articles, that in time the cost will go up, and that at first the increased cost will be borne by the middleman or retailer, until the retailer gets up against the wall, and is compelled to get a newer thing. In many cases a better article could have replaced those articles, provided there had been freedom to do so.

XXII

QUALITY LIKE CHARITY COVERS A MULTITUDE OF SINS

"Some fine and glorious day," says George French, concerning the manufacturers whose methods we are studying, "it will dawn upon even these men that it pays better to cater to the welfare of the people than to shrewdly rob them under the pretense of benefits."

Mr. French describes the process of overcharging the public for the "quality" of nationally advertised goods in a phrase of such felicity that I am envious of the aptness of the words: "to shrewdly rob them under the pretense of benefits."

I do not, however, agree with him that these men will ever discover "that it pays better to cater to the welfare of the people." Perhaps I am too much the pessimist. It will always pay insensitive and unscrupulous men better to rob the public as long as they can, so to speak, pick their pockets within the law and with the blessings of the "fourth estate,"—the newspapers and magazines, which are today their willing procurers in delivering the public to the advertisers. But I be-

lieve it possible to successfully appeal to those who place some value upon self-respect and ask them to consider whether there is not more permanent satisfaction and happiness to be gotten from catering to the welfare of their customers rather than to take advantage of their credulity, suggestibility, and ignorance.

Manufacturers indulge in their huge advertising expenditures for the purpose of increasing the profits of their business. In theory, the increased profits are supposed to come from larger sales. In practice, the increased profits come mainly from the advertiser's ability to overcharge the consumer for the factitious, and sometimes for the purely fictitious, superiority of his goods.

It is well known to all advertising men that it is possible to create a more profitable sale of any article, even though it be identical in quality with competitive articles, if it is effectively advertised. One of the largest advertising agencies in the country, George Batten Company, Inc., of New York, Chicago, and Boston, in a four-page colored advertisement inserted by them in *Printers' Ink,* said upon this subject:

Brown in Boston—
White in New York.

Public buying habits take queer streaks.

In Boston the housewife insists on big brown eggs and will pay an advanced price for them. Mrs. New Yorker must have white eggs, and the wily dealer sorts his eggs

and extracts several cents a dozen more from his patrons for his pale-face eggs.

Thus an old notion handed down from generation to generation forms public opinion as to eggs. It regulates egg commerce.

Any woman on cross-examination will probably admit that an egg is an egg the world over, be it brown or white. The next day she will go out and insist on having either white or brown eggs.

Certain manufacturers who advertise enjoy the same advantages over their competitors as does the little brown hen that lays the big brown egg for Mrs. Boston. They have sensed the fact that the public buys with unreasoning insistence the product with familiar markings, even though it does not know why. Many advertised articles occupy a pedestal because of superior outstanding qualities. But there are unquestionably advertised goods, largely purchased, which have no striking advantage over other goods of equally high quality, except that they are better known and more accessible.

Brown eggs or white eggs are better in public opinion according to what the public has been led to believe. So it is with merchandise. Favorable public opinion for a commodity usually exists in proportion to the insistence and persistence with which the product is advertised.

Here is admission of the fact, by an authority whom advertising men will accept, that an article does not have to be superior to others in order to be profitably advertised. If an article can be profitably advertised in spite of the fact that it is not

superior, then the mere fact that an article has been widely advertised for many years is no assurance whatever of superiority to competitive articles which have not been advertised.

This is an important admission. A very important one if it be considered in connection with the principal advantages claimed for nationally advertised goods. In one form or another it is always claimed that advertised articles are superior in value to those that are not—that they represent better "buys" either because of superior quality or lower price.

In respect to the attractiveness with which they are packaged, advertised articles are conspicuously superior to unadvertised articles. Before an article is nationally advertised the appearance and form of the package in which it is to be sold are very carefully considered. The manufacturer and the advertising agency usually hold conference after conference before, followed by more conferences after the "visualizers," "idea-men," artists, and "copy-writers" have submitted their ideas of the form of package to the manufacturer. Similar conferences dispose of the question of a name for the article, and others of the form of the carton, can, tube, jar, or glass in which the product is to be marketed. The psychological reaction of the prospective customer to the package is carefully investigated, and the convenience of the form of the container is tested sometimes for months and months. The Palmolive Company,

according to *Printer's Ink,* in paving the way for the introduction of its shaving cream, spent eighteen months in various investigations before they placed their new product upon the market. Investigators for the company interviewed one thousand men in all walks of life. They were commissioned to find out what the average man wanted in a shaving cream. When the opinions were collected, the Palmolive Company had its soap-experts evolve a shaving-cream formula that would meet the composite demand of these thousand men, and had its advertising experts evolve a package and an advertising appeal that would most quickly secure the patronage of millions of men like the samplers.

Sometimes the name given to the product has some relation to the product, and sometimes it has not. Palmolive is an example of a name that is descriptive, according to their advertising, of some of the ingredients used in their soaps. But if there were neither palm nor olive oil in their products, it would not be the first time that the name of an advertised article described something very different from the article itself. Grape Nuts, for instance, contains neither grapes nor nuts. It is composed very largely of parched bran. But the name "sounds good." It creates the suggestion of an appetizing product.

Aside from the more attractive packaging of the nationally advertised article, there is only one other form of superiority which may be truthfully

claimed for most advertised articles. When a manufacturer once launches his product, conspicuously identifies it by affixing a distinctive name and attaching to it his trade-mark, he is almost compelled to maintain unimpaired the standard of the article. There are cases in which brands have been changed in their composition without acquainting the users of the brand with the fact that something else is being sold them under the old name. Cases in which formulas, ingredients, processes, and so on, have been changed in this way are sufficiently numerous to prove that it can be done successfully. If the change involved an improvement, the fact would, of course, be widely advertised. If, as has often been the case, the change was made necessary by law or by great advances in the price of some ingredient or process, and the potency or quality lowered by the change, the substitution of the changed article was made and "camouflaged" as skillfully as the peculiarities of the article permitted.

Generally, however, advertised articles are the same in quality, from year to year. They conform to the standard they establish for themselves fairly well. But this standardization is purchased by the consumer at an excessive cost. In order to minimize the fact that he is being charged too much for it, he is urged by one prominent national advertiser to reflect that "the recollection of quality remains long after the price is forgotten." The matter of price, in relation to quality, is the

Achilles heel of the national advertiser. He knows that the consumer can buy a competing article which is not substantially different from his own at a lower price. His cost of selling and advertising prevent him from meeting the price. He is compelled by conditions which he has imposed upon himself to create a demand for his trade-mark so great that the public will buy his brand automatically. He has to create a state of mind in the prospective buyer which will make him believe when shown an advertised article alongside of an identical article that is not advertised, that the advertised article is superior because it is higher in price.

If it be argued that advertised articles cannot be persistently over-priced because customers would not repeat their purchases, it is only necessary to point out that the overcharge must be very large before the public, which is naturally unfamiliar with the technical merits of the article, becomes aware of the overcharge and refuses to buy it.

While instances can be cited in which gross misrepresentation by an advertiser has resulted in the public promptly discontinuing the purchase of the merchandise, few advertisers today make statements so extravagant or so untruthful as to injure the ultimate sale of their goods. The advertiser's agency would be almost certain to advise him as to the extent to which it is safe to exaggerate. The publications in which the adver-

tisements are inserted, in self-defense, censor grossly misleading advertisements as tending to lessen the confidence of their readers in their advertising columns, thus lessening the value of their space to all advertisers. Finally, the "Better Business Bureaus" step in to use moral suasion or sanction the "big stick" of prosecution to restrain flagrant frauds which might lessen the confidence of the public in all kinds of advertising.

National advertising is therefore no certificate of high quality. It is possible to indefinitely sell over-priced, inferior, and even worthless merchandise if the advertising campaign be large enough and shrewd enough, and the article itself not sufficiently important for customers to carefully weigh the question of its merits each time it is bought.

Upon this subject what more can I do than to quote the words of so authoritative a judge of merchandise values as Mr. Edward A. Filene, one of the great merchants of the country:

> I want to put it down as a conviction which has grown out of all the experience of my years in business, that *poor values can be sold by large, persistent advertising.* Witness the immense sale of patent medicines. It is simply a question of psychology—the hammering into people's minds of a certain idea until finally they accept it. If the sacrifice to accept it is not so big as to make a constant re-investigation of that idea necessary —and that is the important part; if it is a thing in common use, that is not extraordinary in price, that does

not force them each time to think out whether they should buy it or whether they should stop and consider if they are really getting full value and really paying only what it is worth, they will submit to the suggestion hammered into their consciousness until it has become almost a part of themselves—that a certain thing, at a certain price, is the best value in the market.

XXIII

HIGH PRESSURE MARKETING IS NON-ESSENTIAL

During the World War, Mr. Julian R. Tinkham, of Upper Montclair, New Jersey, inserted a series of advertisements in the *New York Evening Post* which called attention to the absurdity of permitting advertisers to induce the people to increase the consumption of foods and other essentials while the government was at the same time urgently advocating their conservation. Mr. Tinkham said "Advertising is Non-Essential—Tax it!" At the very time that the government was, as a war measure, striving to curtail all the non-essential activities of the nation and concentrate its man-power upon the essential industries, the volume of advertising increased by leaps and bounds. Thousands and thousands of men rushed into the advertising-supported industries because of the "easy money" flowing in golden streams into advertising to escape the excess-profits taxes.

In attempting to justify the diversion of so much man-power into advertising, *Printer's Ink* published a reply to criticisms like Mr. Tinkham's

which it entitled "Advertising Keeps the World from Starving."

Poor old world! It has had its years of plenty and its years of want, but it has somehow or other managed, in spite of lean years and famine spots, to keep itself alive during all the ages before advertising was invented. But now we are told, it is dependent upon advertising!

In precisely the same way, we are told by all the advocates of high pressure marketing that each and every one of their inventions is essential to the existence of civilized society. We are dependent upon high pressure distribution; we are dependent upon high pressure salesmanship; we are dependent upon high pressure credit. Without manufacturer domination of wholesaling and retailing, there would be no convenient stores to supply what the manufacturers want us to want when and where we desire it. Without the instructions of manufacturer demonstrators and canvassers and salesmen we would not be able to use the products which they have developed. Without installments, presumably, we would be not only without pianos, furniture, and automobiles, but we would also be without clothes—which we are told must be also sold on installments if they are to survive in the face of the competition of the many products which are sold on credit.

Is high pressure marketing really essential to our present existence and future progress? Has it really helped us in any way?

We have seen that, while the cost of producing things has gone down year by year, the price we have had to pay for them has gone up. We have seen the manufacturers of these products spending millions and millions yearly in national advertising. We have unravelled the process by which the high pressure marketing has enabled them to get out of the way of competition and to secure the highest prices for their products that the traffic would bear. We have seen how they have capitalized their profits, and created millions in "good will" by levying a pickpocket's petty tribute upon the unsuspecting public. We have seen how they have raised prices by arbitrarily reducing from time to time the quantity packed in their cartons and cans. We have exposed the fact that they create superiorities for their products which are non-existent, and that when they do exist that they used them for the purpose of grossly overcharging for their goods.

The number of articles and commodities which are being marketed in this way increases every year.

Prices rise as competition changes in one line after another from a "price and quality" basis to an advertising created "consumer demand" basis.

It is getting increasingly difficult for people to think of living at all except in terms of trademarked goods.

The whole economy of our lives has been revolutionized by national advertising.

What are we to do?

When Alexander came to ancient Gordium, the future conqueror of Asia was told that, according to the ancient oracle, whoever succeeded in untying the knot of cornel bark which bound the yoke to the pole of the cart of Gordius should reign over all Asia. Instead of assuming that the oracle required the unravelling of the famous Gordian knot, he cut the knot by a stroke of his sword.

Instead of assuming, in the face of the situation with which consumers are confronted, that Congress must pass some law to tax manufacturers, or to regulate distribution, consumers should simply ignore the manufacturers' propaganda and *stop buying high priced goods whenever it is possible to buy equally as good products for less money.*

If the consumer is purchasing for an average size family, he can, by consistently buying merchandise which is economically marketed, buy precisely the same qualities and quantities of food, clothing, and sundries, and yet save from ten to twenty-five cents out of every dollar he spends.

There is only one rule which consumers must follow.

When an article is nationally advertised, or offered on any other basis than grade, style, and price——stop, look, and listen!

Consumers should give it the "third degree."

First degree: What is the real cost?

Not what is the cost of the package, but what is

the cost of the amount of goods in the package, is the question. A three and a half ounce glass of chipped dried beef which sells for twenty cents may seem like twenty cents' worth of goods, but if the consumer finds out that he is paying over ninety cents per pound for the meat, (which his grandmother thought worth about ten cents a pound), he may decide that he can save himself a whole lot of money by buying his meat in some other form. To determine the real value, he must first learn the cost per pound, per ounce, per quart, per pint, and then compare the cost of the proposed purchase with the price he would have to pay for the same quantity of some other product which could be used with equal satisfaction.

Second degree: Of what does the product consist?

This question may seem like an inquiry as to whether a hungry man ought to eat. So long, however, as manufacturers like to masquerade their product under names that have nothing to do with the goods to which they are attached, it is really a liberal education to learn about the ingredients of which they are composed.

The name of a baking powder tells very little about the ingredients of which it is composed. If a housewife asks for baking powder, and the grocer offers her the choice of three or four brands, isn't it natural for her to buy the baking powder with the most familiar name? But if she asks for a cream of tartar baking powder, and is offered

her choice of three or four brands of cream of tartar powders, she is in position to buy the brand which offers her the best value for her money. She then knows that the ingredients in all the cans being substantially the same, the lowest price powder is the best value. Knowledge of what the product consists is essential if she is to buy a similar product in bulk or packed under some other name.

Third degree: What can be used as an alternative to the extravagantly marketed article, everything considered?

When the consumer buys any article, it is bought for the service which can be secured from it. If the same service can be secured from two different articles, and one article costs less money than the other, the consumer ought to buy the less costly article if only to be able to spend the difference for something that could otherwise not be purchased.

A nationally advertised fat is recommended "For Frying, For Shortening, For Cake Making." These are the services for which the housewife would buy it, but if she can purchase an equally good fat that will render her the same service for less money, why should she pay the "few extra pennies" which the manufacturers admit in their advertising she has to pay every time she buys the nationally advertised fat. The nationally advertised fat is a chemically hardened cotton seed oil. If the manufacturer asks more for it than is

asked for old-fashioned lard, just because he spends a fortune yearly in advertising, there is no good reason for the consumer to blindly accept his own claims about its superiority as a good enough reason to pay higher prices for cooking fat. Why buy one of the cheapest vegetable oils at an excessive price just because the manufacturer has managed to make a passable imitation of lard from it—when it is possible to buy the genuine lard made without the aid of the artificialities of inorganic chemistry? If it is possible to secure the same service from butter, oleomargarine, or lard, and these products are less expensive than the advertised fat, why buy the nationally advertised fat?

This matter of finding substitutes for extravagantly marketed and nationally advertised articles is the real difficulty which meets those who would like to apply the common-sense, which a business man applies to buying for his business, to the buying of things for consumption. Fortunately, when the price of a nationally advertised article is excessive, it is nearly always possible to use an alternative article with equal satisfaction. If one lacks knowledge of a suitable substitute, and has the old American hatred of being "played for a sucker," one can always do without until something that is really either "just as good" or a little better is found.

Locating an alternative article is doubly important when considering the purchase of a newly

advertised product. It is a good plan to let the "easy marks" and the spendthrifts who can afford it, do the experimenting with such products. National advertising is often, it is true, used very effectively for the purpose of educating the public to the uses of some new product. But today it performs this educational function at too high a price. If all national advertising consisted of this sort of educational advertising, the cost of introducing a new article would be greatly reduced. The advertising of new articles would then have the field to itself and would not have to compete for attention with the vast volume of advertising now devoted to "boosting" staple articles.

An army of American housewives applying a judicious skepticism toward nationally advertised articles would promptly shrink the volume of advertising until what remained might perform a useful educational function at a lower cost than the work could be done in any other way.

That the cost of living of any family buying along these lines would be reduced by the amounts saved in buying, is obvious. Suppose, however, that hundreds of thousands of families were to follow the policy I have advocated. What would happen?

There would be a sharp drop in the price of articles now advertised and a sudden increase in the size of their packages. The national advertisers would be forced to meet the competition of

the unadvertised articles on the basis of price and quality or see their brands swept off the markets. No increase in the amount of their advertising would help them to dodge the brutal necessity of honestly meeting the question of "What is your product worth, and how much are you asking for it?" On the contrary, as the advertising would be the very thing which would warn consumers to "Stop, look, and listen," any increase in the amount of their advertising would merely make buyers more cautious and more intent upon locating "the nigger in the woodpile."

Faced with the necessity of reducing the prices on their merchandise, the manufacturers would have to reduce their expenditures for high pressure marketing. There would be a great shrinkage in the amounts appropriated by them for advertising. With the reduction in the volume of advertising, there would be fewer billboards to disfigure our landscapes, while our newspapers and magazines would shrink to convenient sizes. Magazine-monstrosities which, despite the postal regulations, are circulated principally for advertising purposes, would collapse like toy-balloons which had been pricked with a pin. The magazines which desired to survive the change would be forced to improve the quality, rather than as now to increase continually the quantity, of their stories and articles, since they would be forced to rely upon their readers instead of their advertisers for support. They would naturally devote

most of their attention to the interests of the consumers of the country, instead of as now coloring what they print in the interests of their advertisers. "Whose food I eat, his song I sing," is true of our present periodical press. If the food they lived upon came from readers instead of from advertisers, they would find writers who would strikes notes entirely different from prevailing tunes.

With the reduction in the demand for paper to be used for printing magazines and newspapers, our forests would not be sacrificed so rapidly to make paper pulp now being converted into advertising space at the rate of trainloads daily. The conservation of our forests would furnish us lumber for building houses and for furnishing them. What the advertisers and publishers would lose, the consumers of the nation would gain in lower costs of everything into which lumber entered.

The fungus-like publishing and advertising industry would be deflated.

But the biggest deflation would come in the reduction of the terrible price paid by the consumers of the nation for the support of our vast armies of salesmen. Thousands and thousands of salesmen have been recruited over a period of many years from the most aggressive types of manhood produced on our farms and in our factories. For many years energy and constructive thought, which should have been devoted to pro-

duction and transportation, has been devoted to selling and salesmanship.

The salesman is an essential cog in our present machinery of distribution, but we have come to look upon what is merely a cog in the machine as the motive power of the whole process of production and consumption. The salesman who is called a "producer," the man who can get the orders, is considered a more important person in many businesses than the man who can make the goods or the customer for whom they are made. The occupation of the salesman—it is important to bear in mind that all advertising men are fundamentally merely salesmen—has been exalted until in the estimation of the young man of today, selling and advertising rank with engineering, teaching, medicine, and law.

Selling should be an economical method of bringing production and consumption in touch with one another. But national advertising, by increasing the number of brands, and the number of salesmen required to sell the brands, and what is worse, creating army after army of salesmen who have things to sell which are supposed to help the grand army of all salesmen to sell, has added to the cost of distributing merchandise one item after another until the cost of selling exceeds the cost of making the merchandise itself.

The army of salesmen, specialty salesmen, demonstrators, and salesmanagers; the army of advertising men; of salesmen selling magazine,

newspaper, and billboard space; of salesmen selling advertising agency service, and salesmen selling art-work, engraving, electrotypes, printing, and paper, is badly in need of demobilization.

What a healthier and happier nation ours would be if the number of artists, physicians, farmers, and mechanics were increased, and the number of salesmen and clerks decreased! We need lower priced food and less expensive machinery and buildings. We desperately need a more beautiful environment. If that portion of our national man-power which is most adaptable and aggressive, which is now engaged in diverting more and more of the national income into the sterile field of selling, were to be drafted into the arts and crafts and into production and transportation, the whole current of our economic stream would be changed. It would move more slowly, but it would be a deeper stream. What production might lose in speed, would be made up by the increase in its thoroughness, and the quality and durability of the products.

We in this country have overestimated the efficiency of laws as measures of reform, and have underestimated the power of direct action. During the American revolution the efforts of Great Britain to tax our tea were defeated not by the passage of laws in the various colonies, but by the simple expedient of our refusing to buy the tea. Parliament passed laws which, by means of rebates and drawbacks, actually made tea cheaper

in the Colonies than in Great Britain. Yet so effective was the direct action of the colonists that the tea merchants of Great Britain begged Parliament to revoke the taxes long before a single important battle had been fought in the Colonies.

Instead of looking to a law to save us from the economic burden imposed by high pressure marketing, we can save ourselves.

We can simply mark off of our buying lists every product whose maker refuses to sell upon the basis of price, quality, and style in competition with the products of all other manufacturers. Self-interest dictates that we buy in this way. As in almost all cases, enlightened self-interest and the truest public spirit are one and the same.

PART IV

THE ULTIMATE PROBLEM

XXIV

CONSUMER BUYING POWER

Consumer buying power, in the meaning here applied to the phrase, is expenditure for consumption goods.

First of all, it is expenditure. It is not income.

Secondly, it is expenditure of money for merchandise which is almost in its entirety purchased from retailers.

Finally, it is expenditure for consumption goods which are physically removed from the total stock of goods in the market, and which are from an economic standpoint to all intents and purposes destroyed—literally consumed.

Groceries, for instance, are consumption goods which are entirely destroyed by consumers shortly after they are purchased.

Furniture, on the other hand, though it is not destroyed so quickly, still begins to disintegrate the moment it is purchased by the consumer. It disappears by a process of attrition, rather than by a process of mastication.

Even homes—which may be repaired indefinitely by the home owners—are in this sense consumption goods because they are removed from

the realty market, and an equivalent amount of lumber, cement, bricks which went into their building is removed from the total stock of the building materials in that market.

Let me repeat that consumer buying power is not expenditure for capital goods. Capital goods are means and not ends. Looms are bought and mills erected, not because the cotton mills are an objective in themselves, but because they are the means with which manufacturers are enabled to weave cotton goods. If consumers buy cotton goods in sufficient quantity to make investments in cotton mills profitable, purchase of spinning frames, looms, and other necessary machinery by enterprising business men follows sooner or later. If consumers refused to buy cotton goods, artists alone would buy looms and only fools would continue to erect cotton mills.

It is the expenditures of the consumers of the nation for consumption goods that conditions and determines the extent to which it is profitable to build factories and erect machinery in them.

Let the consumers go on a "strike," as they did in 1920, and cease to buy consumption goods and though the farmers continue to produce agricultural products, the factories continue to produce machinery and consumption goods, the builder to build houses, the stream of prosperity will dry up at the source. Very soon the houses, the merchandise, the machinery, the crops become "drugs on the market." Stocks of merchandise accumu-

late in the hands of distributors, orders cease to come to the mills and factories, prices break, and investment in new factories, new mills, and new machinery ceases.

The buyers' strike in 1920 was a dramatic demonstration of the supreme importance of the particular kind of buying power to which I am directing attention—expenditure for consumption. That consumers in city after city should suddenly curtail their buying of almost every line of merchandise—that they should wear overalls as a protest against the high price of clothing—that they should organize protest parades—these things are events which make themselves visible and audible even to the most unimaginative business man. But they are more than mere events. They are portents, the significance of which ought to be understood and appraised by the far-sighted businessman.

How many businessmen really appreciate the fact that the buyers' strike of 1920 has not yet ceased? That consumers are still striking, not deliberately as they did then, but involuntarily, unconsciously? That while they are buying day after day, they are not buying the normal production of our farms and factories?

So far as prosperity is concerned, it makes little difference whether the consumer fails to buy because he deliberately refuses to buy, or because he is unable to buy. In 1920 consumers refused to buy. But, excepting for comparatively short

periods of extremely good times, consumers are always unable to buy all that farmers and factories can produce.

The perfect operation of our present system of production and distribution requires a volume of buying by consumers sufficient to absorb the production of the normal capacity of our industries at prices which include a normal profit.[1]

When consumer buying absorbs all that we normally produce, the products of our factories are sold in sufficient volume to keep wage earners fully employed; the demand for foodstuffs and other agricultural products enables farmers to sell their crops at prices which enable them to buy what they need; our industrial machinery operates at a capacity which pays dividends upon the capital invested in it; in short, the economic machinery of modern civilization operates, not as it usually does, but as it always should.

If consumer buying fails to absorb the normal productive capacity of the nation, then a part of

[1] Since the question of profit has been elevated to a new importance by the publication of "Profits" by the Pollock Foundation, it is desirable to define what is meant by the term normal profit. Normal profit is the amount which has to be added to cost to cover the risks and losses caused by "Acts of God" and the losses inevitable in adjusting production to consumption by changeable human beings. In a perfect competitive economy, the total of normal profits would exactly balance the total of these normal losses. What are generally called profits tend to accumulate and form surpluses in the hands of the richer classes because we have no perfect competitive economy—because special privileges of various kinds, licenses, patents, franchises, trade-marks, and above all our present system of land tenure, make monopoly profits instead of normal profits much more widespread than is generally recognized.

our productive machinery is idle, a part of our capital is idle, and industry has to earn a return upon the entire investment in it from the sale of only a part of what it can produce. Competition between industry and industry, and manufacturer and manufacturer, is abnormally intense. Under such conditions—conditions which prevail at all times except during the peak of a period of prosperity—it is easy to understand why manufacturers turn to high pressure marketing in an effort to create a market for their products.

Since the buying power of the consumers of the nation in what are called "normal" times is insufficient to absorb all that our factories can produce, increased consumer buying power is of supreme importance to economic well being.

Why is it that consumer buying power—expenditures for consumption—does not absorb all that the nation can produce? The advocates of the theory that consumers must be persuaded to consume would answer this question by saying that consumers do not absorb the capacity of our industries because they do not desire the products. A little consideration of the matter will, however, force us to the conclusion that this is not so and that the real reason consumers do not absorb the capacity of our industries is because they can not buy all that they desire.

Consumer buying power can not absorb all that the nation can produce because, (1) prices of merchandise are too high, (2) incomes are insufficient,

and (3) too much of the nation's income is saved. Let me say it in bold letters—*it is not because they do not desire to consume all that can be produced.*

1. The consumer may desire to eat meat three times a day; he may desire to wear silk shirts and ride around in a Rolls Royce automobile, but if the prices of these things are too high, he will not be able to buy them and satisfy his desires. Let them come down in price—and as rapidly as they do, the capacity of the consumer market to absorb all that the manufacturers of them can produce will be demonstrated.

2. Or, let the consumer's earnings be increased. His buying power increases precisely in the same manner as if prices were lowered. He eats more and better food, wears more expensive clothes, buys better furniture, drives a better automobile.

3. What the consumer saves out of his income sets a final limit upon his buying power. The part of his earnings which he does not spend for consumption goods may be placed in a stocking and hidden in a hole in the wall, or be deposited in a savings bank, or invested in stocks and bonds. So far as the market for consumption is concerned, investing his savings sets just as great a limitation upon consumer buying power as does burying his savings in the ground.

The strength of the average consumer's instinct to save, it is obvious, determines his willingness to spend. But the strength of this instinct is in

inverse proportion to the strength of his desire to consume. Here he is vulnerable to attack. His "will to save" is elastic. If only the efforts made be persuasive enough, the producers may induce him to reduce his "savings" margin.

To the extent to which his savings are reduced, buying power is temporarily increased.

But no intelligent person will urge that prosperity be increased temporarily by wiping out the average consumer's instinct to accumulate savings. A hectic prosperity might, indeed, be created by persuading those who have not gratified all their desires to transfer their savings and investments into consumption purchases, but it would be short lived indeed.

Unless all consumer incomes are guaranteed against the vicissitudes of time—unless unemployment, ill-health, and death are abolished—assaults upon the consumers' savings instinct are vicious and dangerous.

But even if it were possible by high pressure advertising and selling to completely destroy the consumers' instinct to save, it would not increase buying power sufficiently to absorb the capacity for production of our factories.

The greater part of the savings out of the nation's income are accumulated by a limited group of consumers who have not the physical capacity to consume much more than they now do. We may expose them to every form of advertising and selling, but nothing can make them eat and drink

and clothe and amuse themselves beyond the physical limitations which nature imposes upon the human animal. Long after they are consuming to the limit of human capacity, their income continues to pile up, and they have to invest it—and add to our facilities for production.

The excess income of the richer one-third of the population and the insufficient income of the poorer two-thirds of the population thus not only result in underconsumption of goods, but in an apparent overproduction of facilities for production.

Under our present economic system, income which is not used for consumption is used mainly for investment. Even if the recipients of unconsumable incomes do not personally invest their surplus in stocks and bonds, but leave it on deposit in their banks, it nevertheless swells the funds available for industrial expansion. The fact that the richer one-third of the population enjoys an income greatly in excess of its ability to buy for consumption, results in an abnormal swelling of funds for speculation and investment in new facilities for production.

To maintain a state of prosperity it is absolutely essential that there be a normal relationship between the rate of saving and the rate of expenditure for consumption. So long as this relationship is normal, it is possible to pay dividends upon the total investments of the country and to keep our extremely complicated industrial machinery in

normal operation. Whenever the ratio of all savings to all consumption is greater than normal, it is obvious that the capacity for production is being increased at the very time when consumption is being decreased.

Existing practice as to the disbursements of their income by the people can be stated in the form of an economic law:

1. *The smaller the income the greater the ratio of disbursements for consumption and the smaller the ratio of savings or disbursements for investments.*

2. *The greater the income, the smaller the ratio of disbursements for consumption and the greater the ratio of savings or disbursements for investments.*

The ratio of investment in new facilities for production to expenditure for consumption goods is a factor contributing to the alternate rise and fall in the business cycle, the importance of which is not recognized. Speculation intensifies the movement, but it does not cause it. If the ratio of savings to consumption were normal and uniform, charts of the state of business would represent straight lines rising with the increase in population and the development of new inventions.

Instead, the tendency for expenditure for capital goods to increase and the expenditure for consumption to proportionately decrease upsets the balance. During the ascending phase of the business cycle, profits are large and investments are

consequently attractive. Larger and larger proportions of the total income thus tend to be diverted to saving, while the proportion available to purchase the ever increasing volume of production becomes relatively smaller and smaller. There finally comes a time when profits, even in spite of rising prices, cannot be realized because a sufficient volume of goods is not being consumed. Then stocks begin to accumulate, production is checked, incomes fall, consumption expenditures decrease, speculations and investment stop, and prices fall during the descending phase of the cycle until bankruptcies and cheap "distress" merchandise enable consumption once again to consume in a normal relationship to capacities for production.

XXV

THE CREATION OF CONSUMER DEMAND

It is not because they do not desire to consume all that can be produced that consumers are unable to absorb all that the nation can produce.

Consumer desires are boundless.

It is true that there is actually a physical limit upon the quantity of food which men may eat and the time that they may devote to wearing out clothes, furniture, and other consumption goods. But the difference in quantity and quality of consumption between individuals in the poorest and individuals in the richest class is so great that no immediate increase of the means of production will enable everybody to consume as much as only the richest consume today.

The potential market for goods—the aggregate unfilled desires of consumers—is infinitely greater than our capacity for production. Human desire seems to be a bottomless pit. We have been pouring goods down that pit in ever increasing quantities and have never yet filled it. We can never satiate the human race. When an old appetite is satisfied, new desires take the place of the old. Time after time, we have multiplied capacity to

produce a hundred-fold. Yet the potential market has expanded and grown beyond our capacity to saturate it.

It is not the potential market which has made me say that our capacity to produce is excessive. It is the insufficiency of immediate demand that makes consumption lag behind production and that makes charts of the state of business consist of alternate peaks and valleys of prosperity and depression. The problem is how to mobilize the potential market—how to convert mere desire into active demand—how to enable it to enter the market place and make the market absorb all that we can ever produce.

The theory which underlies our most conspicuous present day method of converting desire into immediate demand might be called *the theory of the need of persuasion by the manufacturer.* This is the theory that has resulted in the development of national advertising and all those uneconomic methods of distribution which I have called high pressure marketing. If we substitute for the extravagances of persuasion by producers, the economies of supplying and catering to natural demand by retailers, if we operate on *the theory of the normal creation of demand by distributors,* one cause of the rise in the cost of distribution would be eliminated.

Mr. Bruce Barton, a very eloquent and capable advertising man, voices his belief of the need of persuasion by the manufacturer on the ground

that it is a necessary incentive to human progress. He illustrates the need of persuasion by the manufacturer with the following ingenious observations:

> You go in to a savage tribe, and what do you find? You find men who have no wants. You find that the savage is perfectly content if he has a skin to wrap around his loins, another skin to keep the rain off his head, a skin to lie on, and a little food and a fire. So a savage tribe continues for a thousand years and there will be no change. The great-great-grandchildren will be living as their great-great-grandfathers lived. But suppose that out of an airplane an advertising man dropped into that tribe and brought with him pictures of red neckties and tan shoes, and underwear and new hats, and automobiles and bicycles, and feathers and strings of beads. Instantly there would begin in that tribe a transformation. Wants would be kindled, and the desire to satisfy those wants would overcome all other desires, and in obedience to them even a savage is willing to abandon his life of leisure and voluntarily enlist himself in servitude to the creation of a civilization.[1]

Now the only thing that is wrong with this illustration is that it has not the slightest foundation in fact. There is scarcely a single statement which Mr. Barton makes concerning the savage tribe which will stand analysis. It is ludicrous to suggest that they need to be showered with rotogra-

[1] "Advertising and Human Progress," by Bruce Barton, *Advertising and Selling Fortnightly*, November 4, 1925.

vure advertisements of our products. The experience of everybody who has dealt with savages shows that they are quick to grasp for any and every trinket of modern civilization. They have only to be shown mirrors, knives, guns, cloths, phonographs, and all the myriad of products which modern industry so proudly produces to desire them.

The reason the demand for the products of civilization among savages is limited is not because of any lack of advertising to the savages, but solely and simply because the savage lacks the income which will enable him to buy them. The fact that the majority of savages will not engage in sustained labor in order to acquire them is due not to any lack of desire for the products of civilization, but to racial deficiencies or climatic conditions which no amount of advertising will alter. Ignore these limitations of nature, as they have often been ignored by colonists who exploit savages, and the savages wither and die out.

Advertising, if it is successful, enables the advertiser to increase the proportion of business which he does and to decrease the proportion of business which his competitor does, but it can not increase or decrease the total amount of business which is done by all of them. It may shift demand from products of one industry to those of another industry, or from the brand of one manufacturer to the brand of another manufacturer, but it can not increase the demand of the nation

as a whole. A market for one product may be stimulated, but the market for all products is unchanged and, of course, the concomitant to abnormal stimulation of one industry is usually a corresponding decline of another. If by some miracle of advertising, the manufacturers of silk were able to persuade human beings to wear nothing but silk, it is quite obvious that the market for silk would be enormously increased and that for a considerable period of time all the facilities for production in that field would be taxed to their uttermost, but it is also quite obvious that the production of all other textiles would cease. The millions invested in the production of wool and cotton and rayon would earn no returns. What the producers of silk would gain, the producers of other textiles would lose.

The actual methods used in the creation of demand in accordance with the theory of the need of consumer persuasion by the manufacturer have been described in considerable detail in the second part of this book. Branding of the product, national advertising, and high pressure distribution are necessary in order to make it profitable for individual manufacturers to create demand in that way.

Men like Mr. Barton defend this method of converting potential desire into immediate demand and justify all the extravagances of high pressure marketing on the theory that persuasion of the consumer is necessary if he is to use greater quan-

tities of a product or better qualities than he used before. Above all, they claim that such persuasion is necessary if consumers are to use new products.

Persuasion may be necessary. But persuasion by the manufacturer is never necessary in the case of a staple product, and it is doubtful whether it is necessary in the case of many new products. The sheer desire to enjoy the good things of life is so elemental a characteristic of the human beings, that observation of people enjoying good things is sufficient to create a desire for them in the people who do not use or possess them.

Except in the case of new inventions, this potential desire may be converted into immediate demand by simply making the price of the product low enough to bring it within the means of those who may desire it, but who have not been able previously to buy it. But even as to new products which involve considerable demonstration to enable the consumer to use them, it is possible to create demand for them through the medium of the retailer at a much lower cost than through high pressure marketing by the manufacturer.

The retailer is equipped to do this more economically than is the producer. He has first of all direct contact with the consumer. He or his clerks can talk with the customer face to face. He can display the merchandise in his show windows and show cases and demonstrate them in his store and actually permit the consumer to examine the

goods. He can advertise and display and sell new products as an incident to the performance of his economic function of supplying the consumers with the staple and established products they desire and already buy. The producer can not possibly create desire with equal effectiveness. The methods which are open to him all involve costly substitutes for the direct contact which the retailer has with the consumer.

Only in exceptional cases is a manufacturer therefore justified in utilizing high pressure methods in order to create a demand for his products. In the overwhelming majority of cases, it is in the interest of consumers, distributors, and manufacturers that the creation of demand should be the work of the retailers and not of the manufacturers of the country.

Underlying these two theories as to the creation of demand are two totally different conceptions of value. One assumes that a product is worth the price established for it in a competitive market; the other is that the product is worth what the consumer can be made to think it worth. One is an economic conception, and the other is a psychological conception.

In spite of all that has been said by advertising men in defense of the psychological conception, it is at bottom nothing but an ingenious apology for the higher prices charged for advertised, branded goods.

If the psychological conception of value ever

completely prevails, then the present objective method of determining the worth of our products will disappear. Our economic machinery today operates with the minimum of waste and the maximum of equity to both producers and consumers only when there is a common ground upon which values may be determined. Such an objective method of determining the value of our products is furnished us under our present economy only when prices are fixed in a competitive market. We are today moving further and further from the competitive market as a regulator of prices, and as we do so, prices are "pegged" by the manufacturers at levels which permit them to indulge in all the extravagances of high pressure marketing.

XXVI

THE CONSUMER MARKET

When business is dull, business men speak glibly of overproduction because they mistakenly assume that the capacity of the market to absorb goods is the final measure of the capacity of society to consume them. But the capacity of the market is not the capacity of consumption. It is the capacity only of the consuming public's ability to buy.

There can be no such thing as overproduction of any commodity as long as any considerable part of the population wants it but is unable to buy it. It is only when a commodity is not wanted—when tastes and needs have changed—that it is possible to overproduce it.

Mr. C. H. Chase [2] makes the following interesting estimate of production in relation to requirements for the year 1921:

	Per cent of requirement produced
Housing	60
Coal	83
Men's suits	83
Shoes	85

[2] "The Chessboard of Industrial Readjustment," *Searchlight on Congress*, Vol. V, No. 2, July, 1920, p. 23.

Sugar	85
Petroleum	90
Fresh milk	91
Potatoes	92
Beef	95
Wheat flour	95
Commercial building	110
Automobiles	125

Requirements in this table are on the basis of the Ogburn family budget. They are therefore really minimum assumptions. Were requirements interpreted in terms of desires, in terms of potential demand, the actual production of the country would have been still shorter than shown. Yet in the face of the obvious shortage in the production of most commodities, we hear endless talk among so-called practical men about overproduction.

If the inability of the consumer market to absorb the production of our industries is the underlying cause of the intense competition which produces high pressure marketing, the real problem before us is to find the reason for this inability and then devise means of expanding the consumer market.

Modern marketing begins, very properly and sometimes very scientifically, with market analysis. In subject matter, the fundamentals of every market analysis are alike. Whether it is an analysis of a city market, like Philadelphia, or an analysis of the national market, the foreign

market, the farm market, or any other market, it begins with the consideration of such questions as "How many consumers are in that market?" "What is their occupation, sex, age, marital condition?" "What do they now buy?" "What is their buying power?" "How many retailers and wholesalers of various kinds are available as outlets?" Usually it ends with an answer to the question, "How is it possible to most effectively cultivate that market?"

Surely no better method of determining the facts concerning the consumer market can be used than the model method furnished by the modern market analysis. Business has demonstrated the practicability of this method. Business will therefore be able to understand this analysis more readily, and to consider my suggestions without having to learn a new vocabulary and to familiarize themselves with a new idealogy.

In the year 1920, the consumers of the United States consisted of 105,710,620 souls, of whom 33,612,442 were children less than 15 years of age. Of the adult consumers, 36,920,663 were males and 35,177,515 females.

Divorce and apartment hotels notwithstanding, their activities as buyers were principally manifested in family units. There were approximately 24,351,676 such family units—12,803,047 urban and 11,548,629 rural. The average urban family consisted of 4.2 persons; the average rural family consisted of 4.5 persons. Approximately 51,406,-

017 lived on farms and 54,304,603 in cities and towns. There were 9,484,550 urban dwellings with an average number of 5.7 persons per dwelling; and 11,212,654 rural dwellings with an average number of 4.6 persons per dwelling.

In 1923, the estimated income of the people of the United States was $70,000,000,000. This, however, includes an estimate of the value of goods produced and consumed at home. It includes, for instance, the values of home-grown food, such as vegetables, fruits, milk, butter, eggs, poultry, etc., and home-sewn clothing and furnishings, which form a part of the income of those who produce and make these things for themselves, but which is not "money" income and is not passed through the retail trade. If we take into consideration the fact that a very substantial part of the income of our rural population consists of goods which they produce for themselves, it is conservative to estimate the amount of this form of income as 10 per cent. of the total income, or $7,000,000,000.

Deduct this $7,000,000,000 from the total income of $70,000,000,000 and there remains the sum of $63,000,000,000 as the estimated money income of the people of the United States.

This is the aggregate sum of money which the twenty-four million families in the United States received in the form of wages and salaries, as receipts for the products of their farms, as interest on loans, as profits from their businesses, and dividends upon their corporate investments.

What did these families do with it?

About $12,000,000,000 out of that income they saved in some form or other. Some of the savings were deposited in banks, and served to increase the amounts available for the loans and investments which banks make. Some of the savings were represented by the amount of premiums paid to insurance companies in excess of the amounts distributed by the companies to their policy holders. Some of the savings were represented by investments in corporate stocks and bonds, and in land and buildings. And some of the savings were retained by businessmen in their own businesses and used to increase the stocks of merchandise carried or to add to their equipment or to expand their facilities for production by adding new machinery and replacing old and obsolete machinery.

Almost in its entirety, the $12,000,000,000 was used to create a market for capital goods.

About $16,000,000,000 out of the total income was expended for other purposes than consumption goods bought through the retail trades. It was used to pay taxes, to pay rent, to pay for doctors, nurses, dentists; to pay lawyers, and to pay barbers, bootblacks, manicures, and domestics such as cooks, maids, and chauffeurs. Other parts of this sum were expended for hotel, restaurant, and laundry service; for telephone, telegraph, gas, and electrical service; for churches and charities, theaters and movies. This part of

the expenditures of the people of the United States created a market primarily for the services of people who ministered, either individually as in the case of doctors, or in groups as in the case of actors, to the comfort or well being of the people they served.

There remained then about $35,000,000,000 of the annual income which was used to create a market for consumption goods through purchases at retail.

Mr. Paul H. Nystrom[3] estimates the distribution of this expenditure as follows:

Item	Billions of Dollars
Food:	
Groceries and meats, and so forth—including only part sold by retailers	15.8
Clothing:	
Men's, women's and children's—including both ready-to-wear and piece goods, but not value of home dressmaking; footwear, underwear, hats, and so forth, included	7.9
Furniture and House Furnishing:	
Including floor coverings, draperies, curtains, and so forth	2.4
Automobiles, accessories, oil, gas, and so forth. For pleasure purposes only	3.0
Tobacco Products	1.7
Beverages (non-alcoholic), ice-cream, and so forth	.8
Candy and chewing gun	.8
Jewelry, watches, and so forth	.49
Pianos, organs, and so forth	.46
Fur articles	.18
Perfumes and cosmetics	.15
Toilet soaps, and so forth	.15
Miscellaneous	1.17
Total	35.00

[3] "An Estimate of the Volume of Retail Business in the United States," Paul H. Nystrom, *Harvard Business Review,* January, 1925.

If the total money income was $63,000,000,000, then the average family income—the wages, salaries, commissions, and surplus from sales of farm products received by the average family—was $2,625 per year. That does not mean that each family in the United States had an income of that amount. In spite of what the heads of the family with the assistance of "boarders," adult children and far too often minor children, might scrape together, nearly two-thirds of the twenty-four million of families could not buy all of the necessities for normal family life. On the other hand, a very small number of very wealthy families had incomes sufficient to gratify every normal and abnormal human desire. In between were various groups of families, some of them barely able to buy what was needed to maintain a minimum standard of living, while others were able to live in comparative luxury.

Professor Willford I. King[4] divides the population of the United States into four groups in accordance with their money income. The class of population which he calls the poorest received 38.6 per cent. of total income of the nation, but comprised 65 per cent. of the total population. The lower middle class received 14.2 per cent. of the total income and comprised 15 per cent. of the population. The upper middle class, consisting of 18 per cent. of the population, received 26.8

[4] "Wealth and Income of the People of the United States," Willford I. King, p. 235.

per cent. of the total income. While the richest class consisted of only 2 per cent., and received 20.4 per cent. of the total income.

Table IX is a combination of the figures of Professor King, of the number of families, and of the amount of income in 1923 and furnishes us a basis for estimating the amount of income for the average family in each class. These amounts represent very generous estimates of the actual income of each family, especially in the case of families in the poorer classes, because the total income of $63,000,000,000 includes considerable sums which are not distributed to the general population at all, but are retained in business by those corporations which receive the income. However, for the purpose of making clear the argument which follows, the figures are sufficiently accurate.

In Table X, an estimate has been made as to the savings, expenditures for other purposes than consumption goods, and the purchase of consumption goods by each of the four classes of the population.

By dividing the figures in Table X by the number of families in each class, we get the figures in Table XI.

Tables IX, X, and XI make it possible to illustrate the propositions which we shall now develop in an effort to answer the question of *what effect the estimated distribution of the income among the four classes had upon the ability of the entire con-*

TABLE IX

Income of the People of the United States by Classes and Families

Class of Population	Per Cent of Population	Number of Families	Per Cent of Income of Each Class	Amount of Income of Each Class	Amount of Income of Average Family in Each Class
Poorest Class	65	15,600,000	38.6	$24,318,000	$1,559
Lower Middle Class	15	3,600,000	14.2	8,946,000	2,485
Upper Middle Class	18	4,320,000	26.8	16,884,000	3,908
Richest Class	2	480,000	20.4	12,852,000	26,775
All Classes	100[5]	24,000,000[6]	100[5]	$63,000,000[7]	$2,625

[5] Page 235, "Wealth and Income of the People of the United States," by Willford I. King.

[6] Page 155, "*Harvard Business Review*," January, 1925. "Volume of Retail Business," by Paul H. Nystrom.

[7] Estimated income of $70,000,000 in 1923 less $7,000,000 estimated as the value of goods produced and consumed at home.

TABLE X

Expenditures of the People of the United States by Classes

Class of Population	Income of Each Class *		Savings of Each Class *	
Poorest Class	38.6%	$24,318,000	0%	(Negligible)
Lower Middle Class	14.2%	8,946,000	5%	$ 447,300
Upper Middle Class	26.8%	16,884,000	10%	1,688,400
Richest Class	20.4%	12,852,000	77%	9,864,300
	100 %	$63,000,000	19%	$12,000,000

Class of Population	Expenditures for Other Purposes Than Consumption Goods *		Consumer Market Represented by Each Class *	
Poorest Class	25 %	$ 6,079,500	75 %	$18,238,500
Lower Middle Class	27.5%	2,460,150	67.5%	6,038,550
Upper Middle Class	35 %	5,909,400	55 %	9,286,200
Richest Class	12 %	1,550,950	11 %	1,436,750
	25 %	$16,000,000	56 %	$35,000,000

* The following figures are in billions—000 are omitted.

PLATE X

Expenditures of the People of the United States by Classes

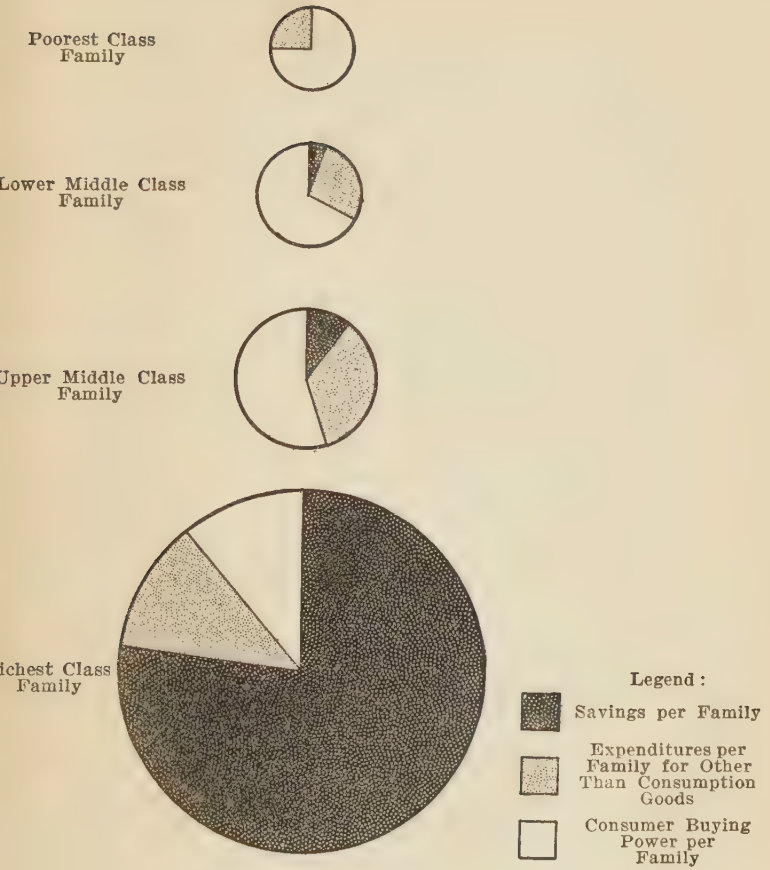


PLATE XI

Expenditures of the People of the United States by Families

TABLE XI

Expenditures of the People of the United States by Families

Class of Population	Number of Families	Income per Family	Savings per Family	Exp. per Family for Other than Cons. Goods	Consumer Buying Power per Family
Poorest Class	15,600,000	$1,559	0	$ 390	$1,169
Lower Middle Class..	3,600,000	2,485	$ 124	683	1,677
Upper Middle Class..	4,320,000	3,908	390	1,368	2,150
Richest Class	480,000	26,775	20,550	3,231	2,993

sumer market to absorb the normal capacity of our producers.

Bearing in mind what has been said concerning desire—concerning the potentialities of consumer demand—is it not clear that out of the twenty-four million families in the United States, only 4,800,000 families—the families in the upper middle classes and the richest class—had incomes which enabled them to purchase all that it was possible for the average family to consume? Only about 20 per cent. of the families were able to contribute an average amount of buying power to the consumer market. Nearly 20,000,000 families, representing 80 per cent. of the capacity for consumption, were unable to buy what they could and would have liked to consume because they lacked the necessary income.

If the 15,600,000 families in the poorest class were to have had incomes which enabled them to buy consumption goods at the same rate as the average family in the lower middle class, the mar-

ket for consumption goods would have increased by $7,924,800,000. This would have meant an expansion of more than 20 per cent. in the volume of goods sold at retail.

If both the poorest and the lower middle classes were to have had incomes large enough to buy at the same rate as the average upper middle class family, the market for consumption goods would have been larger by the enormous sum of $17,006,400,000. This would have meant an increase of nearly 50 per cent. in the volume of goods sold at retail. Instead of consuming thirty-five billion dollars worth of goods in the year, the consumers of the country would have absorbed over fifty billion dollars worth.

A more careful calculation than that which the data at my command has enabled me to make might change these amounts, but such a calculation is just as likely to increase, as to decrease them.

Our manufacturers are engaged in frantic efforts to extend their markets. Many of them indulge in the costly follies of high pressure marketing in the hope of securing for themselves larger shares of the market represented by the wealthier classes of the population and in persuading those classes to consume more and more of their products. Others under the tutelage of the Department of State and the Department of Commerce, try to extend their markets all over the world, overlooking the fact that the products

which they export must be paid for sooner or later with products which we import and that these imports must be sold in the apparently satiated domestic market. Still other manufacturers, when all other methods of extending their markets sufficiently to enable them to operate profitably fail them, turn to the cutting of wages in order to lower prices and thus extend the market, or to the operating of their factories on part time in order to secure high enough prices to operate profitably. And all the time they are overlooking the illimitable possibilities of their own domestic market.

Yet it is plain that the inadequacy of the consumer market is caused by the financial inability of the poorer two-thirds of the population to buy what it might consume, and the physical inability of the richer one-third of the population to consume what it can afford to buy.

Naturally the competition among manufacturers for the possession of the market represented by the purchases of the prosperous one-third of our population is intense. The consumers who form this part of the consumer market have the ability to buy all that the various industries produce, but unfortunately for our manufacturers, they have not the physical capacity for consuming it. Quantitatively, the amount of food and clothing, shelter and entertainment which the average individual can consume is limited. The fact that some peo-

ple can afford to buy more clothing than others, does not necessarily prove that they can actually consume more. With only one-third of our population able to buy all the clothing that they can consume, and two-thirds unable to buy all the clothing that they should, it is a foregone certainty that our wool-growers will produce more wool, our woolen mills produce more cloth, and our manufacturers produce more clothing than the entire consumer market will be able to absorb.

Table X makes it very plain that the bulk of our poorest classes, perhaps 60 per cent. of the total number of consumers, have to live upon incomes too small to purchase the essentials of a decent standard of living for a family in the United States. Obviously these consumers—mainly farmers and unskilled and semi-skilled workers—cannot contribute to buying power what they should if the entire consumer market is to absorb the products of industry. But neither can the bulk of the middle classes. Only the richest classes of families have incomes which enable them to consume as every family should if industry is to be kept normally busy. But the richest classes include only 2 per cent. of the families. In spite of the fact that they can purchase all the essentials and all the luxuries which it is possible for them to consume, they have not the physical capacity to consume enough to make up for the underconsumption of the other classes. Most of

their incomes are therefore saved—and re-invested in additional facilities for production.

An increase of income for the wealthier classes results in no substantial increase in their consumption of food, clothing, or furnishings. It results merely in an increase in their savings and in greater investments for expanding our capacity for production. But an increase in the income of the poorer classes results immediately in an increased demand for food and clothing and furnishings. Anything which enables our poorer classes to increase their buying power enormously increases the market for consumption goods. Every increase in the income of these classes results in practically the entire increase expanding the consumer market. This is an incontestible fact. Men may differ as to the *best means* for increasing the buying power of the poorer consumers, but once they understand the situation, intelligent men cannot differ on the *desirability* of increasing the buying power of the masses. If nothing can be done to dam the stream of consumption goods in which we are being drowned, anything which increases the ability to consume of those classes who are not now consuming to the limit, is an economic virtue. And by the same token, everything which reduces their capacity to consume is an economic crime. Our farmers must receive better prices for their products, because farm families generally are not consuming to the limit. Our wage earners

and white collar workers must be better paid because their families too are not consuming to the limit. And yet prices must be reduced, because lower prices have the effect of enabling those whose incomes are comparatively stable to consume more.

We are thus brought face to face with what is really the central riddle of our present system of economy. Is it possible under the existing economic system to enable the poorer classes to purchase enough so that the consumer market as a whole will be able to absorb all that our factories can produce? Will it be necessary for us to abandon our present conception of private property or to abolish the title of the richest classes to some of the vested rights which enable them to secure so large a proportion of the total income, in order to enable the other three classes to increase their buying power?

An answer to these questions is beyond the scope of this study. I shall content myself with a few suggestions which are designed to show that it is possible to expand the consumer market by (1) lowering prices, thus enabling the poorer classes to buy more; (2) increasing the incomes of the poorer classes and thus enabling them to buy more; and (3) increasing the ratio of expenditure for consumption to expenditure for capital goods, thus both expanding the market for consumption goods and checking the expansion of our capacity for production.

FIRST SUGGESTION—MORE COMPETITION

The first suggestion which I should like to make is that we cease the habit of rendering mere lip-service to the principle of competition.

Ours is supposed to be a competitive system of economy. As a matter of fact, is has become more truly a competition to secure privileges which enable their possessors to operate outside of the competitive market. We are engaged not only in a competition to secure the obvious forms of privilege, such as franchises, patents, and subsidies, but the more insidious forms which are based upon licenses, tariffs, taxation, and nationally advertised trade-marks. All these forms of privilege involve interferences of some kind with the principles of free competition. Each privilege enables someone to set up an internal tariff which restricts the freedom of the market. Prices tend to be higher, because they are based not upon the "higgling" of the market, but upon the principle of charging all that the traffic will bear. If we believe that the competitive system is truly economic, then we should recognize that all these interferences with it are undesirable and, instead of ignoring them, undertake to reduce their numbers and to curtail their extent.

That they can be reduced, if not entirely abolished, by legal and political action is true. But their effectiveness can be very largely reduced without new legislation by the simple expedient

of consistently establishing free markets at every stage of the distribution process.

We have a free market in the distribution of raw cotton, and the price of cotton is determined substantially by competition between buyers and sellers. For the competitive system to work perfectly we must have similar free markets for cotton yarn, gray goods, and finished goods. Prices between grower and spinner, between converter and wholesaler, between retailer and consumer should be fixed by competition unhampered by privileges which enable some factor in the process to ignore the quotations in his market and charge all that the traffic will bear. Such markets require, as has been shown, (1) the establishment of grades and standards, (2) market quotations that become matters of general knowledge, and (3) recognized places in which buying and selling can conveniently take place. Markets of this character do exist for some of the more important commodities and raw materials. They are exceedingly sensitive to fluctuations in supply and demand and they enable buyers to keep prices down to the minimum. But we need desperately markets of this sort for every commodity and for every stage of distribution. Most of the responsibility for uneconomic high prices—prices which check consumption and prevent the consumer market from absorbing the products of our farms and factories—may be traced to the ab-

sence of real competitive markets at the various stages of the distribution process.

SECOND SUGGESTION: MORE CUTTING OF COSTS

The next suggestion which I have to make is that we give serious consideration to the question of reducing unnecesary costs which burden distribution and in this way both free multitudes of workers for really productive effort and expand the market for consumption goods.

Nearly one-fourth of the consumer's dollar paid across the retailer's counter is paid for the transportation of what he buys. Anything which reduces the proportion which he pays for transportation increases by very nearly a corresponding amount the consumer's ability to buy what industry is capable of producing. Consumers buy approximately thirty-five billion dollars worth of goods at retail. About eight billion dollars of this represents direct and indirect payments for transportation. Every one per cent. reduction in the transportation bill would expand the market for the products of our farms and factories by more than eighty million dollars.

Until the year 1917, the cost of transportation per ton mile was constantly being reduced. Since that time it has risen to levels the true significance of which are little appreciated. The subject of lower freight rates should be given earnest consideration by producers because a reduction

in transportation costs would expand the market for consumption goods by more than the full amount of the reduction in rates.

For the same reason that we should lower transportation costs, we should give serious consideration to the effect upon the consumer market of the incidence of taxation.

Our present scheme of taxation is about the most absurd that could well be devised. It burdens the consumer because it results in the passing on of many taxes to the consumer pyramided over and over again, and handicaps the producer both by increasing prices and shrinking the capacity of the consumer market to absorb what he produces. But business men who are harassed with the multiplicity of taxes upon their operations should give real consideration not only to the reduction of taxation, but also to the simplification of this necessary evil. The elimination of many of the forms of taxation which now hamper trade and make monopolistic restrictions common would result in more economic production and distribution and correspondingly expand the market for the products of our farms and factories.

Partly because of the Utopianism with which the subject of the taxation of land values has been advocated, and partly because of the hostility of land speculators to the principle upon which Henry George's idea is based, the fact that it is an economic method of taxation has been overlooked. The taxation of land values may not be a

panacea for all the ills of mankind, but it certainly is a thoroughly practical method for stimulating building and thus of lowering rents. The substitution of land values taxation for other forms of taxation is a policy which is ideally adapted to an individualistic and competitive economic system. Instead of the present policy of more and more government in business, it would mean a policy of less and less government in business.

THIRD SUGGESTION: MORE CONSUMER BUYING POWER

The next suggestion that I should like to make is that our industries should give collective consideration to increasing the buying power of those classes of the population whose incomes prevent them from consuming to their full capacity. We have trade associations and chambers of commerce which give earnest thought and sustained effort to advancing the interests of their members. Why shouldn't they give a little thought to expanding the market for what we produce—not by trying to divert the expenditure of prosperous people, from one industry to another—but by enabling a greater number of consumers to buy what we have the capacity to produce?

The manufacturers of clothing acted in 1926 as if they had only a remote interest in the shrinkage in buying power of the farmers in the corn region caused by the abnormally low prices which farmers received for corn in 1925. It seems to

me that the clothing industry, and every industry for that matter, would have been wiser and infinitely more far-sighted if it had faced the fact that it was to its interest to remedy a state of affairs which prevented these farmer-consumers from purchasing clothing and other consumption goods. Anything which increases the buying power of farmers, wage earners, and all the lower middle classes, increases the capacity of the market to absorb consumption goods. The farmers' organizations which are trying to get higher prices for farm products, are really engaged in extending the market for clothing and for every other product which farmers desire to consume. If as a result of their activities, the farmers have more money to spend, the manufacturers of goods which farmers use are immediate beneficiaries.

Strange as it may seem to manufacturers, this also is true of the activities of the labor unions, especially of those unions which strive to secure higher wages for the poorest paid classes of our workers. These workers are potential consumers of precisely the same quantities of food, clothing, and shelter as their more prosperous and better paid fellow citizens.

If the unions are able to increase their wages, the immediate result is always an increase in the buying power of these consumers. The market for food, clothing, furniture, and every possible commodity which working men consume is expanded. Startling as this may sound to business

men who look upon unions solely with apprehensive regard as to the effect of their activities upon the cost of labor in their own establishments, it is nevertheless undeniable truth.

FINAL SUGGESTION: MORE PATRONAGE OF THE ARTS

The final suggestion which I should like to make may seem a rather fantastic one. And yet none of the suggestions which I have made is grounded upon a more substantial economic basis. If it seems to be somewhat remote from the day to day battle for the market, it is not because it is lacking in practicability, but solely because it is so novel and unusual.

It has, I think, been made clear that one of the principal reasons for the high cost of distribution is the extravagances of high pressure marketing caused by the continuous increase in our production facilities. Each year our capacity for production expands. It expands because the richest classes of the population feel under a social compulsion to invest their excess income. If this excess income were to be diverted by them into other channels than investment, and if it were to be used to increase the buying power of classes of the population who are not now consuming to capacity, it would both expand the market for consumption goods and check the expansion of our capacity for production.

Of the nearly fifteen billions of dollars which we

are saving today, perhaps one-half is needed to replace capital which is lost by obsolescence and depreciation. This means that approximately seven and one-half billions are annually invested to increase our capital structure. A very large proportion of this is used to increase our facilities for producing consumer goods. If one-half of this seven and one-half billion dollars were to be used to adorn and enrich our civilization, it would give employment to nearly one million writers, singers, musicians, artists, sculptors, architects, and craftsmen of all kinds. With each of these the head of an average urban family of 4.2 persons, 4,200,000 persons, whose consumption capacity is now of a much lower order, would increase their consumption in accordance with the increased demand for the services of their breadwinners.

Every time a wealthy man would divert excess income from an investment in a so-called productive enterprise to the purchase of current art, he would, in effect, reduce employments which ultimately result in the manufacture of capital goods and increase the numbers engaged in ministering to culture and the beautiful life. This in turn would have a two-fold consequence; it would reduce competitive extravagances among the producers by checking the increase in productive capacity, and it would expand the consumer market by increasing the total buying power for consumption goods.

The increase in the numbers engaged in professional service and craftsmanship would result in a relative decrease in the numbers engaged in mass distribution and mass production. Reducing the numbers in distribution would lower the cost of distribution and reducing the numbers in production would lower the intensity of competition among producers. The first would directly reduce the cost of living, and the second would indirectly reduce it by making high pressure methods of marketing by manufacturers unnecessary.

The family of the Medici were typical of the wealthy classes of medieval Europe. The Medici, who corresponded economically with our present day captains of industry, devoted great portions of their excess incomes to the support of retinues of artists, sculptors, architects, and musicians, scholars, and poets. The services of poets, artists, and skilled craftsmen were in infinitely greater demand then than in our much wealthier era. The result of this system of liberal support for the fine arts was the Renaissance. Curiously enough, the fact that the wealthiest classes of those days preferred to use their excess income to dot the landscape of Europe with beautiful buildings and to fill them with current productions of artists and sculptors instead of investing them almost entirely in factories—such as there were in those times—has paid their descendants enormous dividends not only in satisfaction, but in cash to this day. Long after the factories, which our wealthy

classes are so busily engaged in building, are crumpled into dust because of changes in the demands of the public, we shall continue to spend good money for the opportunity of seeing the world of art for which the medieval rich used their excess income.

Why shouldn't our wealthy classes indulge in a form of investment which pays dividends such as this? Why shouldn't they occasionally prefer to purchase a painting by a living artist to the purchase of bonds or shares of stock in some promising corporation? Artists are generally more interesting and entertaining fellows than bond salesmen. Our wealthy classes evidently prefer the company of the salesmen because then they can maintain their precious belief that the only practical use for their excess income is investment in business. The day they discover, in sufficient numbers, that there is more sheer joy of life in devoting the bulk of their excess incomes to the enrichment of their environment, they may also make the astounding discovery that real support of living artists, musicians, and scientists will expand the consumer market and at the same time check that menace to all their existing investments—the constant expansion of the capacity for production. Thus they would make the quest of sales less hectic; demand and supply would be more closely equated; prices and business conditions would become more stable; profits more certain and losses less frequent.

But even if more patronage of the arts by itself doesn't result in quite all these desirable developments, there is one thing it is certain to do, and that is make life infinitely more worth while living.

The world—to be a tolerable place for a really civilized people—should consist of only two classes: artists and patrons of artists. It ought to be the ambition of every family to own a few good works of art by contemporary artists, and to live with them in a beautiful home. There ought to be a real market for paintings, sculpture, architecture, music, literature, the teachings of the social sciences and philosophy. There is the mere wraith of such a market in existence today.

I do not mean to imply that all that is needed to produce a nation-wide culture is adequate financial support for the arts. The artist is the product of two forces: his personal genius, and the genius of his audience. To produce great artists, we need great audiences—sensitive, critical, educated audiences. Such audiences would not only support the arts, but they would help to produce the artists.

If our wealthier classes were to really undertake to patronize the arts, in time not only would the patronage of the arts become as fashionable as the patronage of brokerage houses is today, but it would become at least as fashionable among the middle classes and the great masses as is the consumption of nationally advertised food and cloth-

ing, soaps and dentifrices, phonographs and radios.

Strange as it may seem, nothing would more certainly add to the joy of living and lessen the cost of living in what I have called the distribution age.

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